Technical Notes to Draft Amendments to the Income Tax Act

Issued by
The Honourable Marc Lalonde
Minister of Finance

April 25, 1984

Canada

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Department of Finance Canada
Ministère des Finances Canada

These technical notes are provided to assist in an understanding of the amendments proposed to be made to the Income Tax Act and to certain related statutes. They are intended for informational purposes only and should not be construed as an official interpretation of the provisions they describe.

Preface

As has been our practice recently, this publication provides a clause-by-clause technical explanation of each of the proposed amendments to the Income Tax Act and related statutes set out in the draft legislation and press release of April 25, 1984. These amendments cover all of the various income tax measures set out in the Notice of Ways and Means Motions pursuant to my budget of February 15, 1984. The amendments also cover the small business simplification proposals outlined in the February 15, 1984 budget and propose a number of technical amendments to the provisions of Bill C-2 which was enacted on January 19, 1984.

The publication of these notes reaffirms my commitment to the task of ensuring all Canadians a full and equal opportunity to participate in the formulation of tax measures. The technical explanations set out the purpose of each amendment and describe the technical aspects of each change. Accordingly, these notes should assist both Canadians at large and Members of Parliament.

Marc Lalonde

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Minister of Finance

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Employee Benefits – Automobile Operating Costs
ITA
6(2.2)

Clause 1

The Act requires most employment related benefits received or enjoyed by an employee to be included in his income. One such benefit, the automobile "standby charge", relates to the availability of an employer provided automobile for the employee's personal use. The amount of the automobile standby charge is calculated at a monthly rate of 2% of the capital cost of the automobile or two-thirds of the rental cost in the case of a leased automobile. Another such benefit arises where the employer pays for operating costs that relate to the employee's personal use of the automobile. The calculation of this operating cost benefit is presently based on the actual operating costs and number of kilometres driven for personal use. New subsection 6(2.2) introduces an alternative and simpler method for calculating this benefit. Under this method, where an employee notifies his employer in writing before the end of the year, his benefit from employer-paid operating costs will be computed as one-half of the gross automobile standby charge in respect of the automobile. This is reduced by any amount paid by the employee to his employer as a reimbursement of such costs.

This amendment is applicable to the 1984 and subsequent taxation years.

Employee Stock Options

ITA
7(2)

Clause 2

Subsection 7(2) of the Act relates to the application of the rules contained in section 7 dealing with employee stock options in those circumstances where the shares are acquired on behalf of an employee by a trustee. The amendment to this subsection is consequential on the new rule under paragraph 110(1)(d) which allows a deduction for 50% of the benefit included in the income of an employee in respect of qualifying stock options. The amendment to subsection 7(2) ensures that this special deduction will be available to employees in circumstances where qualifying shares are acquired by a trustee on their behalf. The new rules relating to qualifying stock options are described in the commentary on new paragraph 110(1)(d).

This amendment is applicable after February 15, 1984.

Limitation on Employment Expense Deduction
ITA
8(3)(a.1)

Clause 3

Subsection 8(3) of the Act prevents a taxpayer from claiming the employment expense deduction contained in paragraph 8(1)(a) in certain circumstances, including the case where the taxpayer is an "incorporated employee" and a "specified shareholder" of a corporation that has in the year deducted an amount described in subparagraph 18(1)(p)(iii). This is a rule that addresses what are essentially incorporated employment activities. The taxpayer's employment expense deduction is denied in this case because subparagraph 18(1)(p)(iii) permits the corporation to deduct certain employment expenses in computing its income from its business.

The amendment to paragraph 8(3)(a.1) is strictly consequential on the amendment to subsection 248(1) which makes the definition of "specified shareholder" applicable for all purposes of the Act. The amendment simply removes the existing reference to paragraph 125(9)(c). As with the other amendments for simplifying the rules relating to small business, this amendment is applicable for taxation years ending in calendar years commencing after Royal Assent to the implementing legislation.

Inventory Rules

ITA
10(5)(c)

Clause 4

New paragraph 10(5)(c) of the Act is consequential on new paragraph 20(1)(mm) which provides a deduction for the cost of substances injected into a natural reservoir to assist in the recovery of petroleum, natural gas or related hydrocarbons. All or any portion of the cost of such substances may either be deducted in the year the substance is injected or be deferred for deduction in a subsequent year. New paragraph 10(5)(c) provides that where the cost of such substances is deductible under paragraph 20(1)(mm), the substances shall be deemed to be inventory with a cost of nil. Accordingly, paragraph 10(5)(c) ensures that there will be an appropriate inclusion in income should the substance be disposed of at a subsequent time.

This provision is applicable to the 1984 and subsequent taxation years.

Amounts Included in Income

Clause 5

Section 12 of the Act requires the inclusion of certain specifically enumerated items in computing a taxpayer's income for a taxation year.

Subclause 5(1)

ITA 12(1)(v)

Subsection 37(1) of the Act allows a taxpayer to accumulate, or pool, his scientific research expenditures and to deduct them in any year he wishes. Paragraph 12(1)(v) of the Act provides that if the subsection 37(1) pool goes into a negative balance, the negative balance is included in income in order to restore the pool to a nil balance. This paragraph is amended as a consequence of the introduction of the scientific research tax credit mechanism by adding a reference to paragraph 37(1)(g) of the Act to ensure that scientific research expenditures renounced under subparagraph 194(2)(a)(ii) of the Act will be taken into account in determining the negative balance to be included in income. This amendment is applicable to the 1984 and subsequent taxation years.

Subclause 5(2)

ITA 12(1)(w)

Paragraph 12(1)(w) of the Act requires a corporation that carried on a personal services business at any time in the year or a preceding year to include in its income any benefit in respect of a non-interest bearing or low interest loan from an employer that is deemed by subsection 80.4(1) to have been received by it in the year from carrying on such a business. The amendment to paragraph 12(1)(w), applicable for taxation years ending in calendar years commencing after Royal Assent to the implementing legislation, simply replaces the reference to "paragraph 125(6)(g.1)" with a reference to "paragraph 125(7)(d)". It is strictly consequential on the renumbering of paragraph 125(6)(g.1).

Subclauses 5(3) and (4)

These set out the effective dates for the amendments to section 12 of the Act.

Accrued Income on Life Insurance Policies and Annuities
ITA
12.2(4)

Clause 6

Subsection 12.2(3) of the Act provides that individuals must include accrued income on certain annuities and life insurance policies every three years. Subsection 12.2(4) provides an exception to this rule under which individuals may elect to be taxed annually on the accrued income. This subsection is amended, for taxation years commencing after 1982:

(a) to clarify that this election is not available to taxpayers, such as corporations, that are already required to accrue such income annually under subsection 12.2(1),

(b) to allow this election to be made for annuities under which payments have commenced, and

(c) to ensure that a different election can be made subsequently to treat an annuity as a prescribed annuity contract, which is not subject to a requirement to accrue income.

Shareholder Benefits – Automobile Operating Costs
ITA
15(5)

Clause 7

Section 15 of the Act requires the inclusion in income of benefits received or enjoyed by shareholders of a corporation. Subsection 15(5) ensures that the rules relating to the personal benefits from the use of a company automobile are essentially adopted by means of cross-references to the corresponding provisions relating to employee benefits in section 6.

Subsection 15(5) of the Act is amended as a consequence of the introduction of new subsection 6(2.2) which provides a new alternative method of calculating the benefit derived from employer-paid automobile operating costs. The amendment to subsection 15(5) simply extends this new alternative to a shareholder who derives a benefit from corporation-paid operating costs in respect of his personal use of an automobile provided to him by a corporation. The alternative calculation method is described in the commentary under new subsection 6(2.2). This change is applicable to the 1984 and subsequent taxation years.

Small Business
Development Bonds

Clause 8

Section 15.1 of the Act sets out the rules governing the issuance of small business development bonds by certain corporations in financial difficulty.

Subclause 8(1)

ITA
15.1(2)(c)

Subsection 15.1(2) of the Act provides the basic rules that allow interest on small business development bonds to be treated as dividends. Paragraph 15.1(2)(c) provides a special rule for the purpose of computing the cumulative deduction account of a corporation where it has issued such a bond. The repeal of this paragraph is strictly consequential on the elimination of the cumulative deduction account, which is described in the commentary under section 125.

This amendment is applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation.

Subclause 8(2)

15.1(3)(a)

Paragraph 15.1(3)(a) of the Act defines the term "eligible small business corporation" for the purpose of section 15.1 of the Act dealing with small business development bonds.

Generally, to be an "eligible small business corporation" the corporation must be a taxable Canadian corporation all or substantially all of the assets of which are used in an active business. In addition, at the time of the election required in paragraph 15.1(3)(c), the total of the corporation's cumulative deduction account at the end of its preceding taxation year and the cumulative deduction accounts of corporations associated with it must not exceed $750,000 or where the bond was issued after 1981, $1,000,000. As a consequence of the repeal of the cumulative deduction account concept, the amendment to paragraph 15.1(3)(a) removes this cumulative deduction account requirement. This amendment is applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation.

Subclause 8(3)

This sets out the effective dates of the amendments to section 15.1 of the Act.

Prohibition of Certain Deductions

Clause 9

Section 18 of the Act prohibits the deduction of certain items in computing a taxpayer's income for a taxation year.

Subclause 9(1)

ITA
18(1)(p)

A corporation's income from a personal services business represents its income from what is essentially the employment of a specified shareholder of the corporation. In computing this income, paragraph 18(1)(p) generally prohibits deductions with the exception of certain expenses such as salaries and wages paid to an incorporated employee of the corporation.

The amendment to paragraph 18(1)(p) replaces the reference to "paragraph 125(6)(g.1)" with a reference to "paragraph 125(7)(d)" and is strictly consequential on the renumbering of paragraph 125(6)(g.1) as a result of the changes to rules relating to the small business deduction.

Subclause 9(2)

ITA
18(3.2)(b)(ii)

Subsection 18(3.1) of the Act requires the capitalization of most costs incurred by a taxpayer during the period of construction, renovation or alteration of a building where they relate to the construction, renovation or alteration or to the ownership of the land on which the building is located. Subsection 18(3.2) extends this rule to interest expense incurred by persons related to or closely connected with the taxpayer where the interest can reasonably be considered to relate to the construction, renovation or alteration or to the land.

One of the persons subject to this rule is a corporation in respect of which the taxpayer is a specified shareholder within the meaning of paragraph 125(9)(c) of the Act.

As a result of the small business simplification measures paragraph 125(9)(c) is being repealed and the definition of "specified shareholder" is being adopted in subsection 248(1) for the general purposes of the Act. Accordingly, subparagraph 18(3.2)(b)(ii) is amended to delete the existing reference to "paragraph 125(9)(c)".

Subclause 9(3)

ITA
18(5)

Subsection 18(5) of the Act defines certain expressions for the purposes of the "thin capitalization" rules in subsections 18(4) to (6) of the Act. The term "specified shareholder" is defined in subsection 18(5) of the Act but has a different meaning than that adopted for general purposes of the Act in the amendment to subsection 248(1). Consequently, a technical amendment is being made to the opening words of subsection 18(5) to ensure that the "specified shareholder" definition contained in that subsection continues to be applicable for the purposes of subsections 18(4) to (6) of the Act.

Subclause 9(4)

This subclause stipulates that the amendments to section 18 of the Act are applicable to taxation years ending in calendar years that commence after Royal Assent to the implementing legislation.

Deductions Permitted – Business and Property Income

Clause 10

Section 20 of the Act sets out various items that are specifically deductible by a taxpayer in computing his income from business or property for a year.

Subclause 10(1)

ITA 20(1)(ll)

A taxpayer who has made an overpayment on account of his tax payable under either the Income Tax Act or the Petroleum and Gas Revenue Tax Act may receive interest in respect of the overpayment. This interest must be included in the taxpayer's income. However, where it is subsequently determined that the overpayment is not as great as initially determined, provisions in both of these statutes enable the Minister to recover the excess interest received by the taxpayer in respect of the overpayment. Paragraph 20(1)(ll) of the Act provides a deduction in these circumstances to the extent that the excess interest received by the taxpayer was included in computing his taxable income.

Since the various provincial income tax laws may also provide for a recovery of excess interest previously paid to a taxpayer in respect of any overpayment of provincial income tax, paragraph 20(1)(ll) is being amended to permit the deduction of any such excess interest that is in respect of provincial income tax. This amendment is applicable with respect to excess interest repaid after April 19, 1983.

ITA 20(1)(mm)

New paragraph 20(1)(mm) provides a deduction in computing income for the cost of substances injected into a natural reservoir to assist in the recovery of petroleum, natural gas or related hydrocarbons. Commencing with the 1984 taxation year, the cost of any such substance incurred before the end of the year may be deducted in computing income in the year to the extent it has not been otherwise or previously deducted and is not a Canadian exploration expense, Canadian development expense or Canadian oil and gas property expense. This amendment is applicable to the 1984 and subsequent taxation years.

Subclauses 10(2) and (3)

These set out the effective dates for the amendments to section 20 of the Act.

Replacement Property Rollovers

ITA
44(1)(e)(i)(A)
44(6)

Clause 11

Section 44 of the Act provides for the deferral of the capital gain that could otherwise arise on the disposition of certain real property used in a business to the extent that the proceeds of disposition are reinvested in real property used in a similar business.

Subsection 44(1) allows a taxpayer who incurs a capital gain on the disposition of certain business property to defer tax on the gain to the extent that he reinvests the proceeds of disposition in a replacement property within a stipulated time. Subsection 44(6) provides a special rule for a taxpayer who has disposed of a former business property consisting in part of a building and in part of related land. In such a circumstance, the taxpayer may elect, for the purposes of this rollover, to treat any excess of the proceeds of disposition of one such part over the replacement cost of that part as proceeds of disposition of the other part. This would allow, for example, a complete rollover where a taxpayer has moved from a downtown location to a suburban location and replaced old land and a building with new land and a building having a combined cost equal to the proceeds of sale of the old property, even though, the new land is less expensive than the old land and the new building is more expensive than the old building.

The amendments to clause 44(1)(e)(i)(A) and to subsection 44(6) ensure that for purposes of the replacement property rules only that portion of the proceeds of disposition of a property as described above that represents a capital gain in respect of one property may be allocated to another such property.

These amendments are applicable to dispositions of former business properties occurring after February 15, 1984.

Adjustments to Cost Base

ITA
53(1)(m)

Clause 12

Section 53 of the Act sets out the rules for determining the adjusted cost base of a property for the purpose of calculating any capital gain or loss on its disposition. Paragraph 53(1)(m) has been added to the Act to provide that amounts included in computing a taxpayer's income by virtue of the new rules in section 94.1 of the Act relating to offshore investment funds is to be added to the adjusted cost base of such property.

This amendment applies after 1984 when the new rules applicable to offshore investment funds become effective.

Clause 13

Subclause 13(1)

ITA
55(2)(a)

In order to prevent the conversion of capital gains on arm's length dispositions of property into tax-free inter-corporate dividends, subsection 55(2) of the Act in certain circumstances deems all or a portion of such a dividend to be proceeds of disposition of shares and not to be a dividend, except for the purposes of computing the recipient corporation's cumulative deduction account. The amendment to paragraph 55(2)(a) removes this exception relating to the cumulative deduction account. This amendment is strictly consequential on the repeal of the cumulative deduction account concept as part of the changes relating to the small business deduction in section 125.

This amendment is applicable to taxation years ending in calendar years that commence after Royal Assent to the implementing legislation.

Subclause 13(2)

ITA
55(3)(b)

Subsection 55(2) of the Act is a general anti-avoidance provision directed against arrangements designed to use the inter-company dividend exemption to artificially or unduly reduce a capital gain on a sale of shares. It treats the dividends in these situations either as proceeds on the sale of shares or as a capital gain. Paragraph 55(3)(b) provides an exemption from this treatment for certain "split-" reorganizations involving a pro rata distribution of the property of a corporation to shareholders in exchange for shares, commonly called "butterfly" reorganizations.

The existing rules have been interpreted in such a way as to deny the exception on certain butterfly reorganizations the principal purpose of which is not to avoid tax but to distribute assets to shareholders in the course of a bona fide reorganization. This type of transaction should not be subject to the application of subsection 55(2) because it is not in essence a sale of property by one person to another but rather a division of assets held by those persons through one or more corporate intermediaries.

The amendment to this paragraph allows a corporation to distribute assets on a pro rata basis to shareholders except where the corporation or a corporation that it controlled received property in transactions occurring in contemplation of the reorganization other than certain enumerated transactions. These permissible transactions include those enumerated in the closing subparagraphs of the provision and any others that may be specified in the Regulations. The amended rules would expand the scope for reorganizations and would accommodate a transaction where, for example, two or more corporations on a takeover acquire all of the shares of a subsidiary of another corporation which subsequently distributes its property on a pro rata basis to some or all of the new shareholders. As a result, the property of such corporation could be transferred on a rollover basis to the new corporate shareholders. However, the explicit exception for butterfly transactions provided by amended paragraph 55(3)(b) will not apply if the asset distribution is preceded by an issue of shares or debt or other transaction in which property is transferred in a transaction other than those enumerated before and in

contemplation of the reorganization. In most avoidance situations, where the butterfly is designed not to achieve a bona fide reorganization but as an attempt to arrange a tax-free arm's length sale of property, there is a transfer of funds or other property to or for the benefit of the corporation before its assets are distributed.

Revised paragraph 55(3)(b) does not alter the basic purpose intent of the butterfly provision but it does represent a significant technical broadening of the scope for permissible butterflies. The change in these rules is generally effective for transfers of property under paragraph 55(3)(b) after December 31, 1984 but may, if the corporation elects, be effective for butterfly transactions after 1981.

Subclause 13(3)

ITA
55(4)

Subsection 55(4) of the Act provides that a non-arm's length relationship may be ignored where its principal purpose was to avoid the application of the anti-avoidance rule in subsection 55(2). The amendment, effective after 1981, ensures that this rule will apply for the purpose not only of paragraph 55(3)(a) but also of the related corporations test introduced in the amendment to paragraph 55(3)(b).

Subclauses 13(4) to (6)

These set out the effective dates for the amendments to section 55 of the Act.

Annuity Income

ITA
56(1)(d.2)

Clause 14

Paragraph 56(1)(d.2) of the Act provides for the inclusion in income of amounts received from an annuity where the cost of the annuity was deductible in computing income under paragraph 60(l). Paragraph 56(1)(d.2) is being amended to include amounts received from an annuity where its cost was deductible by virtue of new subsection 146(5.5) of the Act. That new provision permits farmers who have attained 71 years of age to take advantage of the new special rollover for up to $120,000 of taxable capital gains on the disposition of farmland. To the extent that such a farmer invests in an annuity described in paragraph 60(l)(ii) of the Act, its cost is deductible from his income as if it were a special RRSP contribution. The amendment to paragraph 56(1)(d.2) ensures that the annuity payments will be brought into income as received in the same way as would payments out of an RRSP.

This amendment applies to the 1984 and subsequent taxation years.

Alimony and Maintenance

Clause 15

ITA 56.1

Under the existing provisions of the Act, only alimony and maintenance payments that constitute an allowance payable on a periodic basis are deductible by the payor and taxable in the hands of a recipient who is the spouse or former spouse of the payor. For this purpose, sections 56.1 and 60.1 treat certain payments made to a third party pursuant to the terms of a court order or written agreement to have been paid to and received by the spouse or former spouse on whose behalf the payments have been made. However, to qualify for the deduction from and inclusion in income, such third-party payments must qualify as an allowance payable on a periodic basis. The application of the existing law to many third-party payments is unclear. The main problem involves the difficulty in determining whether payments covering such expenses as medical bills, tuition fees or mortgage payments constitute an allowance payable on a periodic basis. The amendments to sections 56.1 and 60.1 clarify these issues.

ITA 56.1(1)

The provisions of existing section 56.1 of the Act are being incorporated in new subsection 56.1(1) with one minor amendment. New subsection 56.1(1) clarifies that a qualifying payment to a third party on behalf of a common-law spouse, as defined under the laws of a particular province, must be made pursuant to a court order made under the laws of that province. This clarifying amendment is effective for payments made after 1983.

ITA 56.1(2)

New subsection 56.1(2) deals with third-party payments made after 1983 pursuant to a court order or written agreement for an expense, such as a medical bill, a mortgage payment or a payment of tuition fees. Where the payment is in respect of an expense incurred in the year or the preceding year for the maintenance of a taxpayer who is the payor's spouse or former spouse or the taxpayer's children (provided that they are in the custody of the taxpayer), the new subsection treats the amount as an amount received by the taxpayer as an allowance payable on a periodic basis and thus taxable to the taxpayer if:

1. the expense was incurred at a time when the payor and the taxpayer were separated and living apart,
2. where the expense was incurred for the maintenance of a child in the custody of the taxpayer, the child was not residing with, visiting or otherwise in the charge of the payor at the time the expense was incurred, and
3. the court order or written agreement provides that this new subsection and subsection 60.1(2) of the Act will apply to any payments made pursuant thereto.

An exception to this new subsection provides that the following amounts are specifically excluded from its application:

1. amounts paid in respect of the purchase or improvement of an owner-occupied home of the taxpayer except for amounts of principal and interest paid on a debt in respect of the purchase or improvement not exceeding, in the year, 20% of the original principal amount of the debt, and
2. any other amount paid for the acquisition of tangible property other than an expenditure on account of a medical or educational expense.

ITA
56.1(3)

The existing law requires qualifying alimony and maintenance payments to be received pursuant to a court order or written agreement. One result of this requirement is that payments made before the date of the court order or the written agreement are neither deductible by the payor nor taxable to the recipient. New subsection 56.1(3) alters this treatment by deeming an amount received by a taxpayer in a year to be received pursuant to a court order or written agreement provided that such an order or agreement is made before the end of the following year and the terms thereof indicate that this is the intended result. This new subsection is effective for payments received after 1983.

ITA
56.1(4)

New subsection 56.1(4) provides a definition of an "owner-occupied home" of a taxpayer for the purposes of subsections 56.1(2) and 60.1(2) of the Act. An owner-occupied home of a taxpayer in a taxation year is defined to mean a housing unit that is owned, either jointly or otherwise, and inhabited by the taxpayer at any time in the year. It also includes a share of a cooperative housing corporation. This definition ensures that ordinary mortgage payments made after 1983 by the spouse or former spouse of the taxpayer to a third party in respect of the taxpayer's home may be deductible by the payor and taxable in the hands of the taxpayer only where the property is owned by the taxpayer.

Recapture of Depletion

Clause 16

ITA 59(3.3)(a)

Paragraph 59(3.3)(a) of the Act requires a taxpayer to include in his income 33 1/3% of all amounts receivable by him for property (other than a share, a resource property or depreciable property) or services the cost of which was added in computing his earned depletion base or the earned depletion base of a predecessor. The paragraph is amended to exclude amounts that become receivable by a taxpayer after 1983 if they represent Canadian oil and gas exploration (COGE) expenses on conventional lands. If the amount would be a COGE expense on non-conventional lands at the time it became receivable, the amended paragraph requires no income inclusion for amounts that become receivable after 1984. However for amounts that become receivable in 1984, the rate of income inclusion under this provision is set at 10%. These changes generally ensure that the inclusion in the income of the recipient as a recapture of earned depletion claimed by him will correspond to the earned depletion deduction of the payor. These changes do not apply if the amount would have been a COGE described in subparagraph 66.1(6)(a)(ii) or (ii.1) of the Act in respect of a qualified tertiary oil recovery project.

Paragraph 59(3.3)(a) is also amended so as not to apply to amounts that become receivable in non-arm's length dispositions of property. However, it will apply to any amount that becomes receivable by a taxpayer on the disposition of property the cost of which was added in computing the earned depletion base of a person with whom he was not dealing at arm's length.

59(3.3)(f)

Paragraph 59(3.3)(f) of the Act provides for an income inclusion of 33 1/3 per cent of all amounts receivable by a taxpayer for property (other than a share, a resource property or depreciable property) or services the cost of which was added in computing his mining exploration depletion base or the mining exploration depletion base of a specified predecessor of the taxpayer. The paragraph is amended so that it no longer applies to require an income inclusion by a taxpayer for an amount that becomes receivable by him on the disposition of a property to a person with whom he was not dealing at arm's length. The amended paragraph applies to an amount that becomes receivable by a taxpayer on the disposition of a property the cost of which was added in computing the mining exploration depletion base of a person with whom he was not dealing at arm's length.

In addition, the French version of paragraph 59(3.3)(f) is amended to substitute a more appropriate term for the French version of "mining exploration depletion base".

ITA 59(6)

The amendment to subsection 59(6) adopts prescribed meanings of the expressions "Canadian oil and gas exploration expense", "non-conventional lands" and "qualified tertiary oil recovery project" for the purposes of section 59 of the Act. In addition, the French version of subsection 59(6) is amended to substitute a more appropriate term for the French version of "mining exploration depletion base".

The amendments to paragraph 59(3.3)(a) are applicable with respect to amounts that become receivable after December 31, 1983, the amendments to paragraph 59(3.3)(f) are applicable to amounts that become receivable after April 19, 1983 and the amendment to subsection 59(6) is applicable after April 19, 1983.

Transfer of Pension Benefits

ITA
60(j)

Clause 17

Paragraph 60(j) of the Act permits the tax-free transfer to a registered pension plan or registered retirement savings plan of amounts received by a taxpayer as pension benefits. The paragraph is amended so that only pension benefits that are received out of registered pension plans, that are attributable to services rendered by a person in a period during which he was not resident in Canada or that are received under the Old Age Security Act or Canada or Quebec Pension Plan will qualify for the tax-free transfer. The amendment prevents benefits received out of most unregistered pension plans from being transferred on a tax-free basis to a registered plan. This change is applicable to contributions to registered plans after February 15, 1984 in respect of pension benefits received after that date.

Alimony and Maintenance

Clause 18

ITA 60.1

The provisions contained in section 60.1 of the Act mirror those contained in section 56.1 of the Act. Section 56.1 provides the mechanism for the inclusion in the income of a taxpayer of certain qualifying amounts paid by the taxpayer's spouse or former spouse to a third party on behalf of the taxpayer. Section 60.1 provides the mechanism for a corresponding deduction for the payor. A general description of the provisions contained in sections 56.1 and 60.1 and the main problem addressed by the amendments to these sections is contained in the commentary on the amendments to section 56.1.

ITA 60.1(1)

The provisions of existing section 60.1 of the Act are being incorporated in new subsection 60.1(1) with one minor amendment. New subsection 60.1(1) clarifies that a qualifying payment to a third party on behalf of a common-law spouse, as defined under the laws of a particular province, must be made pursuant to a court order made under the laws of that province. This clarifying amendment is effective for payments made after 1983.

ITA 60.1(2)

New subsection 60.1(2) deals with third-party payments made pursuant to a Court order or written agreement for an expense, such as a medical bill, a mortgage payment or a payment of tuition fees. Where the payment is in respect of an expense incurred in the year or the preceding year for the maintenance of a person who is the taxpayer's spouse or former spouse or that person's children (provided that they are in the custody of that person), the new subsection treats the amount as an amount received by that person as an allowance payable on a periodic basis and thus deductible by the taxpayer if:

1. the expense was incurred at a time when the taxpayer and that person were separated and living apart,
2. where the expense was incurred for the maintenance of a child in the custody of that person, the child was not residing with, visiting or otherwise in the charge of the taxpayer at the time the expense was incurred, and
3. the court order or written agreement provides that this new subsection and subsection 56.1(2) of the Act will apply to any payments made pursuant thereto.

An exception to this new subsection provides that the following amounts are specifically excluded from its application:

1. amounts paid in respect of the purchase or improvement of an owner-occupied home of that person except for amounts of principal and interest paid on a debt in respect of the purchase or improvement not exceeding, in the year, 20% of the original principal amount of the debt, and
2. any other amount paid for the acquisition of tangible property other than an expenditure on account of a medical or educational expense.

ITA 60.1(3)

The existing law requires qualifying alimony and maintenance payments to be paid pursuant to a court order or written agreement. One result of this requirement is that payments made before the date of the court order or the written agreement are neither deductible by the payor nor taxable to the recipient. New subsection 60.1(3) alters this treatment by deeming an amount paid by a taxpayer in a year

to be paid pursuant to a court order or written agreement provided that such an order or agreement is made before the end of the following year and the terms thereof indicate that this is the intended result. This new subsection is effective for payments made after 1983.

Moving Expenses

ITA
62

Clause 19

Section 62 of the Act provides a deduction for the qualifying moving expenses of an individual who moves to a new location in Canada in order to take up employment or start a business. To qualify for the deduction under the present law, the taxpayer must have ceased, before the move, to carry on a business or to be employed at another location in Canada or to be a student in full-time attendance at a post-secondary educational institution. The amendment eliminates the requirements relating to the taxpayer's occupation before he moves. As a result, the amendment ensures that an individual who was unemployed immediately before such a move can claim the deduction for moving expenses. The amendment is applicable to relocations occurring after 1983.

Child Care Expenses

ITA
63(1)

Clause 20

Subsection 63(1) of the Act enables a taxpayer to deduct, in computing his income for tax purposes, certain qualifying child care expenses to the extent that they do not exceed the lesser of $8,000 per family and $2,000 per child. The amendment brings the English version of subsection 63(1) into line with the French version for the 1983 and subsequent taxation years. The French version provides, in conjunction with subsection 63(2), that in the normal circumstances the lower income spouse must claim the expenses. Further, where the taxpayer is separated from the person supporting the children, he may claim the expenses, notwithstanding that he is the higher income earner, but he can only deduct those that he incurs, not those of the supporting person.

Canadian Exploration Expense
ITA
66.1(6)(a)(ii), (ii.1) and (ii.2)

Clause 21

Paragraph 66.1(6)(a) of the Act defines "Canadian exploration expense". This paragraph was amended by Bill C-139 to establish new rules for determining those expenses incurred after 1983 in drilling an oil or gas well that qualify as Canadian exploration expenses. Subparagraphs 66.1(6)(a)(ii), (ii.1) and (ii.2) are amended so that the revised definition will not apply in respect of expenses incurred before 1986. The effect of the amendments is that expenses incurred during 1984 and 1985 in drilling a well which does not go into commercial production within 12 months of completion will be included in the definition of Canadian exploration expense. The expenses incurred after 1985 in drilling such a well will ordinarily be treated as Canadian development expense.

Intergenerational Rollovers on Death

Clause 22

ITA
70(9), (9.1), (9.2) and (9.3)

Subsections 70(9), (9.1), (9.2) and (9.3) of the Act provide rules allowing a rollover of capital gains on intergenerational transfers of farm property from a taxpayer or a spousal trust to a child of the taxpayer as a result of the death of the taxpayer or his spouse. These rules currently require that such property be transferred at its cost amount, thereby effecting a complete rollover of capital gains. The amendments to these subsections permit the spousal trust or the legal representative of the deceased taxpayer to elect to transfer the property at any amount between its cost amount and its fair market value at the time of the death of the taxpayer, or, in the case of a spousal trust, the death of the taxpayer's spouse. The cost of the property to the child will equal the elected amount. As a result of these amendments the rules for transfers of farm property on death will be comparable to the rules for inter-vivos transfers of farm property. These amendments apply to transfers of property after 1983.

ITA
70(9.3)(b)

Paragraph 70(9.3)(b) of the Act allows a transfer, at cost, of a share of a family farm corporation from a spousal trust created by a taxpayer to a child of the taxpayer in consequence of the death of the taxpayer's spouse. A technical amendment to this paragraph provides that a share of a family farm holding corporation will also be eligible for the rollover. This amendment applies to transfers made after May 25, 1978, the date this rollover was originally introduced.

ITA
70(9.6) and (9.7)

New subsections 70(9.6) and (9.7) are added to the Act to provide for a tax free transfer of certain property from a child to a parent where the child dies before the parent. The rules are applicable to farm property and shares of small business corporations in circumstances where the child received the property or shares as a result of the death of his parent or by inter-vivos transfer from his parent. The rules provide that such property can be transferred back to either of his parents for proceeds of disposition equal to an elected amount between the cost amount and the fair market value of the property at the time of the child's death. The cost to the parent will be equal to the elected amount. These amendments apply to property transferred after 1983.

ITA
70(9.8)

Subsections 70(9) and 73(5) of the Act provide rules allowing a rollover of capital gains on the intergenerational transfer of farm property owned by a taxpayer. To qualify, the property must be used by the taxpayer, his spouse or any of his children in the business of farming at the time of the transfer.

Farm property leased by a taxpayer to his corporation or to a corporation or partnership of his spouse or children, does not qualify for the existing rollovers as the property was not used by the farmer or his family in a farming business. These new subsections allow property leased by a taxpayer to his family farm corporation or to a family farm corporation or partnership of his spouse or child to qualify for these rollovers if the property is used in the business of farming by any such family farm corporation or partnership at the time of the transfer. This amendment applies to transfers made after 1983.

ITA
70(10)(a)

Paragraph 70(10)(a) of the Act defines a child of a taxpayer for the purpose of the provisions containing the family farm and small business corporation intergenerational rollovers. This amendment extends the definition of a child of a taxpayer to include a person who was, at any time before he attained the age of 21 years, wholly dependent on the taxpayer and under the taxpayer's custody and control.

This amendment will permit a taxpayer to take advantage of these rollovers where property is transferred to persons such as nieces or nephews where the above criteria are met. This amendment applies to transfers made after 1983.

ITA
70(11)(a)

Paragraph 70(11)(a) of the Act defines the cumulative small business gains account of a taxpayer for the purposes of the capital gains rollover on the intergenerational transfer of shares of small business corporations. This amendment is consequential to new subsection 70(9.7) of the Act concerning the transfer of shares of small business corporations from a child back to his parent as a result of the death of the child. The amendment provides that any reduction in his parent's cumulative small business gains account in consequence of the original transfer to the child will be reversed if the parent reacquires the share as a result of the child's death. This amendment applies to transfers made after 1983.

Employment-Related Loans

Clause 23

Subclauses 23(1) and (2)

ITA 80.4(1)

Subsection 80.4(1) deems an individual or a corporation that carries on a personal services business to have received a benefit in a taxation year in respect of certain employment-related low interest or non-interest bearing loans.

When an individual is deemed to have received the benefit, it is included, under subsection 6(9) of the Act, in his income for the year as income from an office or employment. Where a corporation that carries on a personal services business is deemed to have received the benefit, it is included, under subsection 12(1)(w), in the corporation's income for the taxation year as income from a personal services business.

The preamble of subsection 80.4(1) has been amended by substituting for the reference to "paragraph 125(6)(g.1)" a reference to "paragraph 125(7)(d)". This amendment is strictly consequential on the small business simplification measures.

The amendments to subparagraphs 80.4(1)(b)(ii) to (iv) simply replace the term "entity" with a reference to a "person or partnership" and they are consequential on the repeal of paragraph 125(9)(b) which contained the definition of the term "entity".

These amendments are applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation.

Subclause 23(3)

ITA 80.4(7)(a)(ii)

Paragraph 80.4(7)(a) defines the term "home purchase loan" for the purposes of section 80.4. The amendment to subparagraph 80.4(7)(a)(ii), which is applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation, deletes a reference to "paragraph 125(9(c)" and is strictly consequential on the repeal of that paragraph and the addition of the definition of the term "specified shareholder" to subsection 248(1) of the Act.

Subclause 23(4)

This sets out the effective date for the amendments to section 80.4 of the Act.

Transfer of Property to Corporation

Clause 24

Section 85 of the Act sets out the basic provisions that permit a tax rollover in respect of the transfer of many types of properties to taxable Canadian corporations.

Subclauses 24(1) and (2)

ITA 85(1.1) and (2)

Subsection 85(1.1) of the Act provides that subsection 85(1), which allows for a tax-free transfer of properties to a taxable Canadian corporation in exchange for shares, does not apply to a disposition of a resource property to a corporation that carries on any business before the disposition. This requirement was originally introduced to prevent the offset of the transferee's unclaimed resource expenses against the income from the transferred properties. However other rules operate to address this concern and the requirement in subsection 85(1.1) creates obstacles to achieving a straightforward property transfer. Accordingly, the subsection is repealed with respect to dispositions of property after February 15, 1984.

A consequential amendment is made to subsection 85(2) of the Act to delete the reference therein to subsection 85(1.1). Subsection 85(2) allows the provisions of subsection 85(1) to apply where a partnership transfers property to a corporation.

Subclause 24(3)

ITA 85(7.1), (8) and (9)

In order to qualify for the rollover under section 85, the taxpayer and the corporation must file an election form with Revenue Canada by the date on which the income tax return for the year of the transfer is required to be filed. However, an election filed within 3 years of that date will be accepted if accompanied by payment of the late-filing penalty provided in subsection 85(8) of the Act. The introduction of new subsection 85(7.1) and the amendments to subsections 85(8) and (9) will permit the Minister of National Revenue to accept elections filed after the 3-year deadline where in his opinion it would be just and equitable to do so. In addition, the Minister will be empowered to accept amendments to elections already filed. In either case a penalty will be exigible of 1/4 of 1% per month of the amount by which the fair market value of the transferred property exceeds the elected amount, to a maximum of $8,000. These amendments apply to elections filed after February 15, 1984 and to amended elections filed after that date.

Subclauses 24(4) and (5)

These set out the effective dates for the amendments to section 85 of the Act.

Clause 25

Section 87 of the Act deals with the tax treatment applicable to the amalgamation of two or more taxable Canadian corporations. For the most part section 87 maintains the tax positions of the predecessor corporations in the amalgamated company.

Subclause 25(1)

ITA
87(2)(j.2)

New paragraph 20(1)(mm) of the Act provides a deduction in computing income for the cost of substances injected into a natural reservoir to assist in the recovery of petroleum, natural gas or related hydrocarbons. The amendment to paragraph 87(2)(j.2) of the Act allows a new corporation formed on an amalgamation to deduct such costs that were incurred but not deducted by a predecessor corporation. This amendment is applicable to the 1984 and subsequent taxation years.

Subclause 25(2)

ITA
87(2)(y)

Paragraph 87(2)(y) of the Act provides for the flow through of the cumulative deduction accounts of predecessor corporations to the new corporation on an amalgamation. The repeal of paragraph 87(2)(y) is strictly consequential on the repeal of the cumulative deduction account concept as part of the small business simplification measures. The amendment is applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation.

Subclause 25(3)

ITA
87(2)(z)

The amendment to paragraph 87(2)(z) is consequential on the introduction of the extended carryover period for foreign business-income tax credits under section 126 of the Act. The amendment permits an amalgamated corporation to continue to claim the unused foreign tax credits of its predecessor corporations. Accordingly for purposes of carrying forward unused foreign tax credits, paragraph 87(2)(z) provides that an amalgamated company will be considered to be a continuation of its predecessors. This amendment applies in computing tax for the 1984 and subsequent taxation years.

Subclause 25(4)

ITA
87(2)(ee)

Paragraph 87(2)(ee) of the Act provides for the flow through of the preferred-rate amounts of predecessor corporations to the new corporation on an amalgamation. The preferred-rate amount represents that portion of a corporation's retained income that has benefited from the small business deduction. This concept is relevant for the purposes of the special tax under Part VI of the Act designed to recapture the benefit of the small business deduction where a corporation becomes non-resident controlled.

The repeal of paragraph 87(2)(ee), applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation, is consequential on the repeal of the Part VI tax as part of the small business simplification measures.

Subclauses 25(5) to (7)

These set out the effective dates for the amendments to section 87 of the Act.

Winding-up of a Corporation

Clause 26

Subsection 88(1) of the Act sets out rules relating to the tax rollover that is generally available in respect of taxable Canadian corporations on the winding-up of a subsidiary into a parent corporation that owns at least 90% of the subsidiary's shares.

Subclauses 26(1) and (2)

ITA 88(1)(e.2)

Under paragraph 88(1)(e.2) many of the detailed rules to be applied on a winding-up of a subsidiary into its parent are established by way of cross-reference to the corresponding provisions in section 87 relating to amalgamations. The cross references in paragraph 88(1)(e.2) and subparagraph 88(1)(e.2)(ix) of the Act concerning the foreign tax credit are repealed for the 1984 and subsequent taxation years as a consequence of the introduction of new paragraph 88(1)(e.7) which provides a separate rule to "flow-through" a subsidiary corporation's unused foreign tax credits following a winding-up.

A further amendment to paragraph 88(1)(e.2) of the Act deals with the flow-through of a subsidiary's preferred-rate amount to its parent on a subsection 88(1) winding-up. This amendment to paragraph 88(1)(e.2) is applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation. It deletes all references to the subsidiary's preferred-rate amount and is strictly consequential on the repeal of Part VI of the Act.

Subclause 26(3)

ITA 88(1)(e.3)

Paragraph 88(1)(e.3) of the Act provides that a subsidiary's cumulative deduction account is added to that of its parent where the subsidiary has been wound-up under subsection 88(1). The repeal of paragraph 88(1)(e.3), applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation, is strictly consequential on the repeal of the cumulative deduction account concept as part of the small business simplification measures.

Subclause 26(4)

ITA 88(1)(e.7)

Paragraph 88(1)(e.7) is added to the Act as a consequence of the introduction of the extended carryover for unused foreign business-income tax credits under section 126 of the Act. This amendment will permit a parent corporation to claim the unused foreign tax credits of its subsidiary following a winding-up. To the extent that a subsidiary's unused foreign tax credit for a year has not been deducted it will be considered to be an unused foreign tax credit of the parent for the parent's taxation year in which the subsidiary's taxation year ended. This rule ensures that on a winding-up the carryforward period for the subsidiary's unused foreign tax credit for any particular taxation year will be maintained in the parent corporation. This amendment is applicable in computing tax for the 1984 and subsequent taxation years.

Cross-Reference

ITA 88(1.1)

The coming into force provision governing the flow-through of losses on the winding-up of a subsidiary corporation into its parent is amended by clause 87 (see commentary thereunder).

Subclause 26(5)

ITA 88(1.3)

Subsection 88(1.3) of the Act deems a parent corporation to have been in existence during the period in which its subsidiary was in existence in order to permit the parent to carry forward the charitable donations and losses of its subsidiary that were not deducted before it was wound-up. The amendment to this subsection extends the same rule to unused foreign tax credits of a subsidiary and is consequential on the amendments to section 126 of the Act relating to the extended carryover period for foreign business-income tax credits. This amendment is applicable to the computation of tax for the 1984 and subsequent taxation years.

Subclauses 26(6) to (9)

These set out the effective dates for the amendments to section 88 of the Act.

Elections for Foreign Affiliates

Clause 27

Subsection 93(1) of the Act permits a corporation resident in Canada to treat proceeds received on the sale of shares of a foreign affiliate as a dividend rather than as proceeds of disposition. This allows the corporation to obtain the benefit of any exempt or taxable surplus that relates to the share of the foreign affiliate which has been disposed of without the affiliate actually declaring a dividend.

ITA
93(5)

In order to qualify for the subsection 93(1) election, a corporation is generally required to file an election form with Revenue Canada on the date on which its income tax return for the year of the sale is to be filed. However, the Minister of National Revenue is required to accept an election filed within 2 years of that date if it is accompanied by payment of the penalty provided under subsection 93(6) of the Act. Because the information required for an election may be difficult to generate within this period, the amendment to subsection 93(5) of the Act extends the late-filing period to 3 years. This amendment is applicable to elections filed after February 15, 1984.

ITA
93(5.1), (6) and (7)

The introduction of new subsection 93(5.1) and the amendments to subsections 93(6) and (7) will permit the Minister of National Revenue to accept elections filed under subsection 93(1) after the 3-year deadline provided in amended subsection 93(5) where in his opinion it would be just and equitable to do so. In addition the Minister will be empowered to accept amendments to elections already filed. In either case a penalty of 1/4% per month of the elected amount, to a maximum of $8,000, will be exigible. These amendments are applicable to elections filed after February 15, 1984 and to amended elections filed after that date.

Offshore Investment Funds

Clause 28

ITA 94.1

New section 94.1, applicable after 1984, contains an anti-avoidance provision relating to investors in offshore investment funds. This provision applies where a taxpayer has invested in an offshore investment fund and one of the main reasons for such investment was to reduce or defer the tax liability that would have applied to the income generated from the underlying assets of the fund if such income had been earned directly by the taxpayer. In such a case the taxpayer is required to include an amount in income determined by applying the prescribed rate of interest to the designated cost of his interest in the fund.

ITA 94.1(1)

Subsection 94.1(1) contains the main provisions relating to this anti-avoidance rule including the definition of offshore investment fund property, the factors that will be considered in determining whether or not one of the main reasons for the investment was to reduce or defer income taxes and the method for computing the amount of income from the investment that is taxable in the hands of the investor.

Paragraphs 94.1(1)(a) and (b) provide a definition of "offshore investment fund property". This is defined as a share of the capital stock of, an interest in, or a debt of, a non-resident entity or an interest in or a right or option to acquire such a share, interest or debt where its value is primarily related to portfolio investments in the categories of asset listed in subparagraphs 94.1(1)(b)(i) to (ix). A taxpayer's interest in a non-resident entity that is a controlled foreign affiliate is not subject to these provisions since the affiliate's investment income is already subject to accrual taxation under the provisions relating to foreign accrual property income. The legislation also permits the prescription of certain non-resident entities or classes of non-resident entities that will not be subject to these provisions.

In order for section 94.1 to apply to a taxpayer's investment in an offshore investment fund property, it must be established that one of his main purposes for acquiring or holding the investment was to reduce or defer taxes. Some of the factors set out in the provision that are to be considered in determining the existence of such a motive include the nature, organization and operation of the non-resident entity, the extent to which the income from its portfolio assets bears significantly less tax than would have been payable had the income been earned directly by the taxpayer and the extent to which such income is distributed by the non-resident entity as it is earned.

Where an intention to reduce or defer Canadian income tax has been established, the taxpayer is required to include an amount in his income in respect of the property. The amount to be so included for a year is calculated by first multiplying the "designated cost" of the property at the end of each month in the year by one-twelfth of the prescribed interest rate applicable at that time. The total of these products is the amount that is required to be included in the taxpayer's income for the year. In order to prevent double-taxation, the amount required by this section to be included in a taxpayer's income is reduced by distributions or other amounts in respect of the property (other than capital gains) that are required by any other provision of the Act to be included in the taxpayer's income for the relevant year.

The term "designated cost" is defined in subsection 94.1(2). The prescribed interest rate is that used generally for purposes of the administration of the Act and is currently 10% per annum.

ITA
94.1(2)

Subsection 94.1(2) contains two definitions for the purpose of applying subsection 94.1(1). The first is "designated cost" to a taxpayer of an offshore investment fund property (paragraph 94.1(2)(a)). It is defined as the aggregate of:

(i) the cost amount to the taxpayer of the property determined without reference to any income imputations under section 94.1,

(ii) the amount by which the fair market value of the property exceeds its adjusted cost base at the end of 1984,

(iii) all amounts included in the taxpayer's income under subsection 94.1(1) in respect of the property for previous taxation years, and

(iv) where amounts made available by any person to another person after 1984 increase the fair market value of the property in excess of any increase in the cost amount of the property, the amount of such excess.

An additional rule in paragraph 94.1(2)(a) states that where an offshore investment fund property is prescribed by regulation, its designated cost is treated as nil so that no income will be imputed on such property. It is proposed that an offshore investment fund property acquired by a taxpayer by way of bequest or inheritance from a non-resident person immediately after and as a consequence of the non-resident's death will be prescribed for this purpose.

The other definition in subsection 94.1(2) is that of a "non-resident entity". It is defined to be a non-resident corporation or a trust, partnership, organization, fund or entity not resident or situate in Canada.

Foreign Accrual Property Income

ITA
95.(1)(b)(ii.1)

Clause 29

Paragraph 95(1)(b) of the Act defines "foreign accrual property income". New subparagraph 95(1)(b)(ii.1), applicable after 1984, is added to the Act as a consequence of the addition of the new provisions relating to offshore investment funds. It provides that for purposes of computing the foreign accrual property income of a controlled foreign affiliate, the provisions in section 94.1 relating to offshore investment fund property will apply as if the words "earned directly by the taxpayer" in subsection 94.1(1) were replaced by the words "earned by the person resident in Canada in respect of which the taxpayer is a foreign affiliate". The effect of this amendment is to ensure that where a controlled foreign affiliate has an interest in an offshore investment fund, the income therefrom will be treated as foreign accrual property income and as such attributed to and included in the income of those residents who control the affiliate.

Late-filed and Amended Elections

ITA
96(5.1), (6) and (7)

Clause 30

Subsections 97(2) and 98(3) of the Act permit a tax rollover on the transfer of property to or from a Canadian partnership in certain circumstances. The partners may elect to have these rollover provisions apply by filing a prescribed form with Revenue Canada by the date on which the tax return for the year of the transfer is to be filed. However, an election filed within 3 years of that date will be accepted if accompanied by payment of the late-filing penalty provided in subsection 96(6) of the Act. The introduction of new subsection 96(5.1) and the amendments to subsections 96(6) and (7) of the Act permit the Minister of National Revenue to accept elections filed under subsections 97(2) and 98(3) after the expiry of the 3-year late-filing period where in his opinion it would be just and equitable to do so. In addition, the Minister will be empowered to accept an amendment to a previously-filed subsection 97(2) election. Subsection 96(6) is amended to provide for the penalties to be paid on acceptance of these elections. These amendments apply to elections filed after February 15, 1984 and to amended elections filed after that date.

Trust Income

ITA
104(29)

Clause 31

Subsections 104(6) and (13) of the Act provide a deduction from the income of a trust and an inclusion in the income of a beneficiary for income of the trust payable to the beneficiary. In this manner, the tax liability of the trust in respect of such income is flowed through to the beneficiary. Since payments under the Petroleum and Gas Revenue Tax Act, Crown royalties and certain related payments are not deductible in computing income, the flow-through under subsections 104(6) and (13) may not be fully available to a trust making such payments. In these circumstances the trust will not normally have a corresponding amount of cash available to pay out.

New subsection 104(29) permits a trust to designate an amount not exceeding a specified fraction of this "phantom income" as payable to its beneficiaries for the purpose of section 104. The proportion of this amount payable to each beneficiary must also be designated by the trust. This proportion must be reasonable given the various rights of the beneficiaries to receive the income of the trust as determined under trust law. It should be noted that the operation of subsections 104(8) and (25.1) will have the effect of restricting a designation in favour of a "designated beneficiary" as defined in subsection 104(8).

Subsection 104(29) applies to the 1982 and subsequent taxation years. Designations in respect of 1982 and 1983 phantom income may be made by a trust in its 1984 tax return, but a designation for either of these years is only effective in respect of a beneficiary who concurs in writing with the designation.

Cross-Reference

ITA 104

The coming-into-force provision of a Bill C-139 change to paragraph 104(6)(b) of the Act is being amended by clause 86 (see commentary thereunder).

Personal Exemptions

ITA
109(1)(e)

Clause 32

Section 109 of the Act sets out the various deductions for personal exemptions. Paragraph 109(1)(e) allows a taxpayer to claim a personal exemption in respect of a niece or nephew who is resident in Canada and wholly dependent upon the taxpayer. The existing deduction is available only if one of the following conditions is met:

(1) the mother of the dependant was separated from her husband and not in receipt of support in respect of the dependant,

(2) the father of the dependant was mentally or physically infirm, or

(3) the father of the dependant is deceased and the mother has not remarried.

The amendment to this paragraph, applicable to the 1984 and subsequent taxation years, removes these conditions relating to the status of the parents of the nieces and nephews.

Deductions in Computing Taxable Income

Clause 33

Subclauses 33(1) and (2)

ITA 110(1)(c)

Paragraph 110(1)(c) of the Act allows a deduction in computing the taxable income of a taxpayer for medical expenses in excess of 3% of the taxpayer's income for the year. Effective for the 1984 and subsequent taxation years, this paragraph is amended to add three new categories of expense that will qualify as medical expenses. These are the cost of cloth diapers and disposable briefs for persons who are incontinent by reason of illness, injury or affliction, the expenses incurred for the purchase, care and maintenance of a hearing-ear dog trained to alert profoundly deaf persons and certain costs incurred to train the deaf person in the handling of such dogs. In addition, the Income Tax Regulations are to be amended to include in the list of prescribed medical devices a power-operated lift prescribed by a medical practitioner to assist a disabled person in entering and leaving a vehicle.

Subclause 33(3)

ITA 110(1)(d)

Currently where an employee of a corporation, other than a Canadian-controlled private corporation, acquires a share pursuant to a stock option offered by his employer, he is deemed to receive, as income from employment in the year he acquired the share, a benefit equal to the amount by which the fair market value of the share at the time of the exercise of the option exceeds the exercise price. Similar rules apply where the employee has sold the option rather than having purchased the shares.

New paragraph 110(1)(d) of the Act allows a deduction in computing taxable income of one-half of the stock option benefit included in calculating income from employment where an employee exercises or disposes of a qualifying stock option granted after February 15, 1984. A stock option will qualify if, at the time the option is granted, the exercise price is not less than the fair market value of the shares at that time, the employee deals at arm's length with the grantor and the shares are described in subsection 192(6) of the Act. However, the time limitations for the issue of shares as set out in subsection 192(6), which defines "qualifying shares" for the purposes of the share-purchase tax credit will not apply for purposes of paragraph 110(1)(d) and qualifying shares are not required to be shares of taxable Canadian corporations. Shares of corporations other than the employer corporation will also qualify if the other conditions are met and the corporations are members of a related group.

New paragraph 110(1)(d) is applicable to qualifying stock options granted after February 15, 1984.

Subclauses 33(4) and (5)

ITA
110(1)(e) and (e.2)

Paragraphs 110(1)(e) and (e.2) of the Act allow a special medical expense deduction with respect to a person who, by reason of illness, injury or affliction, is confined to a bed or wheelchair for a substantial period of time each day throughout any 12 month period ending in the year. The amount of this deduction for 1984 is $2,480. The existing deduction is not available for the year in which the person first becomes so confined. These paragraphs are amended for the 1984 and subsequent taxation years to allow this deduction in the year that the person becomes confined to a bed or a wheelchair provided he is so confined for the remainder of the year and, in the opinion of a medical practitioner, is likely to be so confined for at least 12 months.

Subclause 33(6)

ITA
110(2.2)

Subsection 110(2.2) of the Act provides a special rule for gifts of tangible capital property to a charity. It allows the donor of such property to elect to have an amount less than its fair market value treated for tax purposes both as the proceeds of disposition of the property and as the amount of the donation. The amendment to this subsection extends this special rule to a non-resident taxpayer who after February 15, 1984 makes a gift of Canadian real property to a prescribed non-resident charity provided that the property is to be used in the public interest.

Subclause 33(7)

ITA
110(8)(c)

Paragraph 110(8)(c) of the Act defines ''registered charity''. A registered charity may be a charitable organization, a private foundation or a public foundation. This definition is amended to require a charity to be registered after February 15, 1984, as a charitable organization, private foundation or public foundation. This definition will also apply to registered charities that are designated by the Minister of National Revenue after February 15, 1984 pursuant to new subsection 110(8.1) or (8.2).

Subclause 33(8)

ITA
110(8.1)

New subsection 110(8.1) of the Act allows the Minister of National Revenue to designate a charity that was a registered charity on February 15, 1984 as a charitable organization, private foundation or public foundation. Such a designation may only be made before the end of the charity's first taxation year commencing after 1983. Once the charity is notified of such designation by registered letter, it is considered, for taxation years commencing after 1983, to be registered as a charitable organization, private foundation or public foundation, as the case may be, unless and until a subsequent designation is made by the Minister or its registration is revoked. This designation is necessary in order for existing registered charities to comply with the amended definition of ''registered charity'' in paragraph 110(8)(c). Under subsection 172(3), a registered charity is provided with a right of appeal in respect of the designation.

ITA
110(8.2)

New subsection 110(8.2) of the Act allows the Minister of National Revenue, for taxation years commencing after 1983, to designate a registered charity as a charitable organization, private foundation or public foundation and, upon notification by registered letter, the charity will be considered, for taxation years commencing after the date of notification, to have been registered as such. The Minister may make this designation on his own initiative or upon application by the registered charity. This designation will remain in force unless and until the registration of the charity is revoked or a subsequent designation is made by the Minister. Under subsection 172(3), a registered charity is provided with a right of appeal in respect of a designation or a refusal to make a requested designation.

Subclauses 33(9) to (12)

These set out the effective dates for the amendments to section 110 of the Act.

Non-Capital Loss

ITA
111(8)(b)(i)

Clause 34

Paragraph 111(8)(b) of the Act defines the "non-capital loss" of a taxpayer for a taxation year. The amendment to subparagraph 111(8)(b)(i) is consequential upon new paragraph 110(1)(d) which allows a special deduction in computing taxable income equal to 50% of the benefit from employment received by an employee in respect of the exercise or disposition of certain qualifying stock options. The amendment to subparagraph 111(8)(b)(i) simply ensures that a taxpayer's special 50% deduction under new paragraph 110(1)(d) will be recognized in computing any non-capital loss he may have for the year.

This amendment is applicable to the 1984 and subsequent taxation years.

Taxable Income of Non-residents

ITA
115(1)(d)

Clause 35

Subsection 115(1) of the Act defines the amount of taxable income earned in Canada on which a non-resident is subject to tax under Part I of the Act. In computing such taxable income, paragraph 115(1)(d) permits a non-resident to claim certain of the deductions from income in computing taxable income that are available to residents of Canada. Paragraph 115(1)(d) is amended to allow non-residents to claim the deduction provided in new paragraph 110(1)(d) of the Act relating to certain qualifying employee stock options. Consequently, a person who exercises a qualifying stock option at a time when he is not a resident of Canada will be able to deduct 50% of the stock option benefit in computing his taxable income. This places the non-resident on the same basis as a resident with respect to the net inclusion in taxable income relating to such options. This amendment is applicable to the 1984 and subsequent taxation years.

Clause 36

Subclause 36(1)

ITA
120.1(2)(b)

Paragraph 120.1(2)(b) of the Act sets out the rules that apply when a taxpayer dies in a year in which he has a pool of forward-averaged income – his "accumulated averaging amount" – which has not been brought back into taxable income. The amendment to this provision in Bill C-2 provided that a taxpayer's accumulated averaging amount would be taxed in the year of his death as if 1/3 of the amount had been included in taxable income in each of the three years preceding the year of death by means of elections under subsection 110.4(2) made for each of those years. Subsection 110.4(2) provides the rule which permits a taxpayer to elect to bring amounts forward-averaged in one year into taxable income in a subsequent taxation year. The Bill C-2 amendment was defective in its application to the accumulated averaging amount of an individual who died before 1985 in that an election under subsection 110.4(2) is only effective in respect of the 1982 and later taxation years. The reference to subsection 110.4(2) is removed by the present amendment to paragraph 120.1(2)(b). The effect of this change is to permit any accumulated averaging amount remaining at the end of the year of an individual's death to be taxed as if 1/3 thereof were added to taxable income in each of the 3 preceding years. As a result the estate may obtain a refund of the forward-averaging tax previously paid. This amendment is applicable to the 1982 and subsequent taxation years.

Subclause 36(2)

ITA
120.1(3)

Subsection 120.1(3) deals with the circumstances where a taxpayer who makes a forward-averaging election for a year is not a resident in a province at the end of the year and is therefore not ordinarily subject to provincial income taxation. In these circumstances, the tax credit under subsection 120.1(1) and the tax added under subsection 120.1(2) are allocated to the province of residence and increased by 47%. This increase, set at the percentage referred to in subsection 120(1) of the Act, ensures that the total tax additions and credits approximate the amount that would be the combined federal and provincial tax if the individual were resident in a province. However, for the 1983 and subsequent taxation years the forward-averaging tax and credit will be allocated between the provinces in the same proportion that the taxpayer's tax otherwise payable is allocated. Accordingly, subsection 120.1(3) is amended for such years to provide that the additional 47% only applies to that portion of the federal forward-averaging tax or credit that the taxpayer's business income not earned in a province bears to his total income.

Subclause 36(3)

ITA
120.1(5)

Subsection 120.1(4) provides the mechanism to permit the forward-averaging tax credit to which an individual is entitled in a year to be refunded to him to the extent that it exceeds the amount of his tax otherwise payable for the year. Under subsection 120.1(5) the amount of the forward-averaging credit that is refunded in a

year to an individual resident in the Province of Québec on the last day of a taxation year is reduced by 16.5%. This is the aggregate of the special Québec abatements – 3% under subsection 120(2) of the Act and 13.5% under the special cost sharing arrangements relating to the financing of certain established programs. For the 1983 and subsequent taxation years, the forward-averaging credit will be allocated between the provinces in the same proportion that the taxpayer's tax otherwise payable is so allocated and a consequential amendment to subsection 120.1(5) ensures that this 16.5% reduction of the refund will apply to a taxpayer in the same proportion that his income earned in Québec is of his total income.

Subclauses 36(4) and (5)

These set out the effective dates for the amendments to section 120.1 of the Act.

Overseas Employment Tax Credit

ITA
122.3(2)(b)

Clause 37

Amendments enacted under Bill C-2 provide that for the 1984 and subsequent taxation years an individual's entitlement to the federal tax reduction under subsection 120(3.1) of the Act is to be reduced by 10% of the amount by which his tax otherwise payable exceeds $6,000. For this purpose the tax otherwise payable is defined to be net of the overseas employment tax credit as provided in section 122.3 of the Act. A problem of circularity arises because the overseas employment tax credit is itself based on the tax otherwise payable net of the federal tax reduction. To avoid this problem the definition of tax otherwise payable for the purposes of the overseas employment tax credit is being amended to exclude the reference to the federal tax reduction.

Cross-Reference

ITA 122.3

In addition the coming into force provision governing the overseas employment tax credit is amended by clause 88 (see commentary thereunder).

Small Business Deduction

ITA 125

Clause 38

Section 125 of the Act contains the rules concerning the small business deduction that may be claimed by a Canadian-controlled private corporation in respect of its income from carrying on an active business in Canada. Major amendments are being made to simplify the operation of this important section of the Act. These amendments will apply to taxation years ending in calendar years that commence after Royal Assent to the implementing legislation. The three basic changes being made as part of the simplification of section 125 are as follows:

- the total business limit and the cumulative deduction account concepts are being repealed thereby removing the existing $1,000,000 income accumulation cap above which a corporation or a group of associated corporations ceases to qualify for the small business deduction;
- the concept of non-qualifying business income is being repealed with the result that such income will qualify for the full 21% small business deduction; and
- the rules relating to a corporation that carries on an active business in Canada as a member of a partnership are being substantially simplified.

ITA 125(1)

As amended, subsection 125(1) will continue to provide the basic rules for calculating a Canadian-controlled private corporation's small business deduction for a taxation year. Under this subsection, the corporation's small business deduction will be equal to 21% of the least of the following amounts:

- its net income for the year from active businesses carried on by it in Canada;
- its taxable income for the year (net of foreign income not taxed in Canada as a result of the foreign tax credit system); and
- its business limit for the year which is $200,000 unless it is associated with another Canadian-controlled private corporation in the year or has a short taxation year.

ITA 125(1)(a)

A corporation's net income for the year from active businesses carried on by it in Canada is determined under revised paragraph 125(1)(a) as the amount, if any, by which the aggregate of

- its income for the year from all active businesses carried on by it in Canada other than as a member of a partnership, and
- its "specified partnership income" for the year which under new paragraph 125(7)(f) is defined to be its eligible income for the year from all active businesses carried on by it in Canada as a member of a partnership,

exceeds the aggregate of

- its losses for the year from all active businesses carried on by it in Canada other than as a member of a partnership, and
- its "specified partnership loss" for the year (which under new paragraph 125(7)(g) is defined to be its eligible losses from all active businesses carried on by it in Canada as a member of a partnership).

The determination under new paragraph 125(1)(a) differs from the determination under existing paragraph 125(1)(a) in two significant ways. First, under the existing provisions, two sets of rules apply for determining the amount of eligible income earned by a corporation as a member of a partnership. One rule applies in respect of partnerships to which the corporation is not ''joined'' in the year and another rule applies in respect of a group of ''connected'' partnerships to which the corporation is ''joined'' in the year. Under the new formulation, one general rule applies in respect of every partnership of which the corporation is a member. Under this rule, a corporation includes in its ''specified partnership income'' the total of all amounts each of which is the lesser of its active business income from a partnership and that proportion of $200,000 that its share of the partnership's income is of the total income of the partnership.

The second difference is the elimination of an anomaly regarding losses. Under existing paragraph 125(1)(a), where a corporation has income from an active business carried on by it in Canada as a member of a partnership and also carries on one or more non-profitable active businesses, the losses may, in some cases, serve first to reduce the income that qualifies for the small business deduction instead of reducing the income subject to tax at the normal corporate tax rate. New paragraph 125(1)(a) ensures that a corporation's losses from an active business carried on by it in Canada will reduce the amount of its active business income taxable at the normal corporate tax rate before reducing the amount of such income that is taxable at the preferential small business tax rate.

ITA
125(2) to (5)

The amended subsections 125(2) to (5) of the Act continue to provide rules for sharing the small business deduction among Canadian-controlled private corporations that are associated. The current provisions are essentially maintained subject to two exceptions. First, a corporation will not have a ''total business limit'' under the new rules so that there is no apportionment of this amount. Second, a new rule concerning the calculation of a corporation's business limit for a short taxation year is introduced in paragraph 125(5)(b). This provision applies to all corporations, whether or not associated, and requires a proration of the limit for any taxation year of less than 51 weeks duration. It provides that a corporation's business limit for such a taxation year is its limit otherwise determined multiplied by the number of days in the taxation year over 365.

ITA
125(6)

The section 125 definitions that are currently found in subsection 125(6) are being adopted in revised subsection 125(7). Amended subsection 125(6) is an anti-avoidance provision designed to prevent the use of multiple partnerships to artificially increase a corporation's small business deduction. This subsection applies where it is reasonable to conclude that the separate existence of the partnerships is not solely for the purpose of carrying on their businesses in the most effective manner and one of the main reasons for their separate existence is to effect an increase in the amount of the claim for the small business deduction of any corporation. In such cases, the excess small business deduction is eliminated by stipulating that the corporation and each corporation with which it is associated may only include in its specified partnership income for a year its active business income from the partnership that earned the greatest amount of income for any fiscal period ending in the year.

ITA
125(7)(a) to (c)

As amended, subsection 125(7) provides definitions for the terms used in section 125. Most of these terms are currently defined in subsection 125(6). The following

definitions have been carried forward without any change from subsection 125(6): "active business", defined in new paragraph 125(7)(a); "Canadian-controlled private corporation", defined in new paragraph 125(7)(b); and "income of the corporation for the year from an active business", defined in new paragraph 125(7)(c).

ITA
125(7)(d) and (e)

The definition of "personal services business", (new paragraph 125(7)(d))), and of "specified investment business", (new paragraph 125(7)(e)) are based on the definitions currently found in paragraphs 125(6)(g.1) and (h), but they have been modified. The new versions allow any full-time employee in the business to be included in meeting the existing six full-time employee test so as to qualify the business for the small business deduction. Under the existing provisions, an employee who is a "specified shareholder" of the corporation or related thereto cannot be included in counting full-time employees for the purpose of determining the nature of the business. The term "specified shareholder" is defined in existing paragraph 125(9)(c) and generally means a person who owns at least 10% of any class of shares of the corporation, either directly or through a trust or partnership.

In addition, the definition of "specified investment business" in new paragraph 125(7)(e) adopts the provisions contained in existing subsection 125(11). This ensures that the full-time employees test will continue to be satisfied where an associated corporation provides managerial, administrative, financial, maintenance or other similar services to the corporation and it is reasonable to conclude that the corporation would have employed more than five full-time employees if those services had not been provided.

ITA
125(7)(f)

The specified partnership income of a corporation for a year is added to the corporation's income for the year from active businesses directly carried on by it in Canada to obtain its total income for the year from active businesses for the purpose of calculating its small business deduction. The specified partnership income of a corporation for a year is the aggregate of two components. The first component consists of the corporation's eligible share of the income from each partnership to which it belongs from all active businesses carried on by it in Canada as a member of that partnership for each fiscal period of the partnership ending in the year. The eligible share is the lesser of the corporation's share of the income from all active businesses carried on by it in Canada as a member of the partnership and that proportion of $200,000 that its share of the partnership income is of the total income of the partnership. The second component is an addition to ensure that any losses of the corporation for the year from active businesses carried on by it in Canada are offset first against business income that is not eligible for the small business deduction before reducing the income that would otherwise qualify for the small business deduction. This second component will be relevant only if the corporation has both losses in the year from an active business carried on by it in Canada and income for the year from an active business carried on by it in Canada as a member of a partnership.

ITA
125(7)(g)

The specified partnership loss of a corporation for a year is the total of the corporation's share of the losses from the active businesses carried on in Canada by it as a member of a partnership for each fiscal period of the partnership ending in the year. This amount is added to the corporation's losses for the year from active businesses carried on directly by it in Canada to obtain its total losses for the year from active businesses for the purpose of calculating its small business deduction for the year.

Tax Credit for Manufacturing and Processing Profits
ITA
125.1(1)

Clause 39

Subsection 125.1(1) of the Act provides a tax credit in respect of Canadian manufacturing and processing income so as to reduce the general corporate income tax rate on such income to 20% where it is eligible for the small business deduction and to 40% in other cases.

The amendments to this subsection are applicable to taxation years ending in calendar years that commence after Royal Assent to the implementing legislation. They are strictly consequential on the changes to the small business deduction rules and simply delete the existing reference to paragraph 125(1)(d).

Foreign Tax Credit

Clause 40

Residents of Canada are subject to tax under the Income Tax Act on their world income. In order to prevent double taxation where foreign-source income is also taxed in another country section 126 of the Act permits a credit against tax for income taxes paid to a foreign jurisdiction. The foreign tax credit may not exceed the amount of Canadian tax otherwise payable on the foreign-source income.

Foreign taxes levied on the income of a taxpayer from carrying on a business in a foreign jurisdiction – "business-income taxes" – are claimed as a tax credit under subsection 126(2). The existing Act permits unclaimed business-income taxes paid for a year to be carried over to be included in calculating the taxpayer's foreign tax credit for any of the 5 following taxation years.

Subclause 40(1)

ITA
126(2)(a)

The amendment to paragraph 126(2)(a) of the Act provides that a taxpayer's unused foreign tax credits may be carried back three years and forward seven years for purposes of computing his foreign tax credit for the 1984 and later taxation years. An "unused foreign tax credit", which is the amount of his business-income tax paid for a year that is not deductible in that year as a foreign tax credit, is defined in new paragraph 126(7)(e).

Subclause 40(2)

ITA
126(2.3)

New paragraph 126(2.3)(a) provides that the amount of foreign tax credit claimed in a taxation year will be considered first to be in respect of foreign taxes paid for that year and that any remaining balance of foreign tax credit claimed is considered to be a deduction in respect of unused foreign tax credits carried over from other years. Paragraph 126(2.3)(b) provides that unused foreign tax credits must be utilized in the order in which they arose. For example, an unused foreign tax credit in respect of a particular country for the 1985 taxation year must be applied before a 1986 unused foreign tax credit in respect of that country. New paragraph 126(2.3)(c) ensures that an unused foreign tax credit deducted in one year may not be claimed again in a subsequent year.

Subclause 40(3)

ITA
126(7)(b)

Paragraph 126(7(b) of the existing Act defines the "foreign- tax carryover" of a taxpayer for a taxation year. This term will not be used under the new foreign tax credit carryover rules. Accordingly paragraph 126(7(b) is repealed for the 1984 and later taxation years.

Subclause 40(4)

ITA
126(7)(e)

New paragraph 126(7)(e) defines a taxpayer's "unused foreign tax credit" for purposes of the extended foreign tax credit carryover under subsection 126(2). An

unused foreign tax credit in respect of a country for a taxation year is the amount of business-income tax paid to that country for the year that cannot be claimed in that year as a foreign tax credit.

Subclauses 40(5) to (7)

These set out the effective dates for the amendments to section 126 of the Act.

Investment Tax Credit

Clause 41

Subclause 41(1)

ITA 127(9)(d.4)

Subsection 127(9) of the Act defines the investment tax credit of a taxpayer at the end of a taxation year. Paragraph 127(11.1)(c) sets out the investment tax credit rates to be used in calculating a taxpayer's investment tax credit with respect to qualified scientific research expenditures incurred by him in his taxation year that includes November 1, 1983 or in a subsequent taxation year in which he has not deducted the special incremental research allowance under section 37.1 of the Act.

Under the existing provisions, where the expenditures are incurred by a Canadian-controlled private corporation that is eligible for the small business deduction, subparagraph 127(11.1)(c)(i) provides that the investment tax credit rate is 35% in respect of such expenditures. For corporations that do not meet this test, subparagraph 127(11.1)(c)(ii) operates to provide that the rate is generally 20%. The effect of the existing rule is to confine the special 35% rate in respect of such expenditures to Canadian-controlled private corporations that alone, or together with members of an associated group of corporations, have a cumulative deduction account of less than $1,000,000.

The repeal of the cumulative deduction account requires that new conditions be introduced with respect to the eligibility of a corporation to the special 35% rate of investment tax credit on qualified scientific research expenditures. Under the amendments, the 35% credit will be restricted to Canadian-controlled private corporations or associated groups of such corporations where the taxable income for the year does not exceed $200,000. A further limit will restrict the application of the 35% rate to the first $2,000,000 of the corporation's or group's annual qualifying scientific research expenditures.

New paragraph 127(9)(d.4) is applicable to taxation years ending in calendar years that commence after Royal Assent to the implementing legislation. It replaces subparagraph 127(11.1)(c)(i) and introduces the $200,000 taxable income and the $2,000,000 annual expenditure limit into the calculation of investment tax credit. It permits a Canadian-controlled private corporation or such corporations that are members of an associated group of corporations that have met the income test to add in computing its investment tax credit for a taxation year an amount in respect of its qualified scientific research expenditures made in the year and referred to in paragraph 127(11.1)(c). The amount that may be added in computing such a corporation's investment tax credit represents the excess of the 35% credit over the credit already included in respect of the expenditures eligible for the special 35% rate. The rule permits the taxpayer to make the addition in respect of such qualified expenditures as he chooses provided that in aggregate they do not exceed his annual expenditure limit.

ITA 127(9)(d.5)

New paragraph 127(9)(d.5) is applicable to taxation years ending in calendar years that commence after Royal Assent to the implementing legislation and is strictly consequential on the addition of new paragraph 127(9)(d.4) to the Act. It provides for an inclusion in computing a taxpayer's investment tax credit at the end of a taxation year of an amount equal to the amount of the investment tax

credit that was included, under new paragraph 127(9)(d.4), in computing the taxpayer's investment tax credit at the end of the 7 taxation years immediately preceding and the 3 taxation years immediately following the year.

Subclause 41(2)

ITA
127(10.3)
to (10.6)

New subsections 127(10.3) to (10.6) define a Canadian-controlled private corporation's "expenditure limit" for a taxation year for the purposes of new paragraph 127(9)(d.4) of the Act. The addition of these subsections is applicable for taxation years ending in calendar years that commence after Royal Assent to the implementing legislation. The new subsections provide a $2,000,000 annual limit on scientific research expenditures eligible for the special 35% rate of investment tax credit and are patterned on the business limit allocation rules in subsections 125(2) to (5) of the Act.

Subsection 127(10.3) sets a Canadian-controlled private corporation's "expenditure limit" for a taxation year at $2,000,000 unless it is associated in the year with one or more other Canadian-controlled private corporations in which case, unless it has filed an agreement provided for in subsection 127(10.4), its expenditure limit for the year is nil. Subsection 127(10.4) provides that if all the Canadian-controlled private corporations of a group that are associated with each other in a taxation year file with the Minister of National Revenue an agreement whereby, for the purposes of paragraph 127(9)(d.4), they allocate the $2,000,000 expenditure limit to one or more of them for the taxation year and the aggregate of the amounts allocated is not more than $2,000,000, the expenditure limit for the year of each of the corporation's is the amount allocated to it. Subsection 127(10.5) of the Act provides that if any of the Canadian-controlled private corporations of a group that are associated with each other in a taxation year has failed to file the agreement within 30 days after notice in writing by the Minister has been forwarded to any of them that such an agreement is required, the Minister shall, for the purposes of paragraph 127(9)(d.4), allocate the $2,000,000 expenditure limit to one or more of them for the year and the expenditure limit for the year of each of the corporations is the amount so allocated to it by the Minister.

Subsection 127(10.6) provides two additional rules with respect to the determination of a Canadian-controlled private corporation's expenditure limit for the purpose of paragraph 127(9)(d.4). Paragraph 127(10.6)(a) provides that where a Canadian-controlled private corporation has two taxation years ending in a calendar year and it is associated in each of those taxation years with another Canadian-controlled private corporation that has only one taxation year ending in the calendar year, the expenditure limit for the first mentioned corporation for its second taxation years is nil. Paragraph 127(10.6)(b) provides that where a Canadian-controlled private corporation's taxation year is less than 51 weeks, its annual expenditure limit for the year is that proportion of its annual expenditure limit for the year otherwise determined that the number of days in the year is of 365.

ITA 127(11.1)(c)

Subclause 41(3)

As described in the note on new paragraph 127(9)(d.4), paragraph 127(11.1)(c) of the Act sets out the investment tax credit rates to be used in calculating a taxpayer's investment tax credit with respect to qualified scientific research expenditures incurred by him in his taxation year that includes November 1, 1983 or a subsequent taxation year where the taxpayer has not deducted the special incremental research allowance under section 37.1 of the Act in the year.

The amendment to subparagraph 127(11.1)(c) of the Act, which is applicable to taxation years ending in calendar years that commence after Royal Assent to the implementing legislation, repeals subparagraph (i) thereof and is consequential on the addition to the Act of new paragraph 127(9)(d.4).

Subclause 41(4)

This sets out the effective dates for the amendments to section 127 of the Act.

Refundable Investment Tax Credit

Clause 42

ITA 127.1(2)(a)

Section 127.1 of the Act provides for the refundability of a portion of unused investment tax credits earned in the period commencing on April 20, 1983 and ending on April 30, 1986. The refundable portion referred to as the "refundable investment tax credit" is defined in subsection 127.1(2). In the case of individuals, certain trusts and Canadian-controlled private corporations that are eligible to claim a small business deduction by virtue of having a cumulative deduction account of less than $1,000,000, 40% of the unused investment tax credit is refundable. For other taxpayers, 20% of the unused credit is refundable.

With the repeal of the cumulative deduction account, new conditions must be met by a corporation in order to qualify for a 40% rate of refund in respect of unused investment tax credits. The amendment to paragraph 127.1(2)(a) stipulates that to qualify for the 40% refund rate, the corporation must be a Canadian-controlled private corporation throughout the year and the aggregate of its taxable income for the year and the taxable incomes of all corporations with which it was associated in the year for their taxation years ending in the calendar year must not exceed the aggregate of their business limits for those years.

ITA 127.1(2)(d)

Paragraph 127.1(2)(d) of the Act sets out the amounts included in computing a taxpayer's investment tax credit for a taxation year that are to be taken into account in computing the taxpayer's "refundable investment tax credit" for the same taxation year. The amendment to that paragraph simply adds a reference to new paragraph 127(9)(d.4) and is strictly consequential on the addition of that paragraph to the Act.

The amendments to paragraphs 127.1(2)(a) and (d) are applicable to taxation years ending in calendar years that commence after Royal Assent to the implementing legislation.

Share-Purchase Tax Credit

Clause 43

Subclause 43(1)

ITA 127.2(3.1)

Subsection 127.2(3) of the Act permits a trust to allocate its share-purchase tax credit to its beneficiaries. This flow-through mechanism is not intended to be available to trusts exempt from tax and trusts governed by an employee benefit plan or a revoked deferred profit sharing plan. Existing paragraph 146(2)(c.4) of the Act relating to registered retirement savings plans and analogous provisions dealing with other types of tax-exempt trusts may operate to trigger revocation of their exempt status in circumstances where such an allocation is made. This is because the allocation of share-purchase tax credit can be viewed as a benefit conferred on the beneficiary that arises as a result of the existence of the trust.

New subsection 127.2(3.1) clarifies this matter by preventing these trusts from allocating credits. This restriction is necessary to prevent beneficiaries from withdrawing funds from such a trust in the form of credits on a tax-free basis. This amendment does not prevent certain exempt trusts from continuing to qualify for the refund of their share-purchase tax credits pursuant to subsection 127.2(2) of the Act. This change is applicable after the date on which the draft legislation was made public.

Subclause 43(2)

ITA 127.2(6)(b)

Paragraph 127.2(6) of the Act defines the unused share-purchase tax credit of a taxpayer for a taxation year. The amendment to this paragraph simplifies the definition and ensures that, as intended, the unused share-purchase tax credit for a taxation year consists only of that portion of the credits acquired in that year that could not be utilized in the year. This change is applicable to the 1982 and subsequent taxation years.

Subclause 43(3)

ITA 127.2(10)

Under section 127.2 of the Act, only the first registered holder, other than a broker or dealer in securities, of a share qualifies for a share-purchase tax credit. In response to recent representations that this creates difficulties in the marketing of public share issues, new subsection 127.2(10) permits the first purchaser, other than a broker or dealer in securities, of a share of a public corporation to qualify for the share-purchase tax credit. To qualify under the "first purchaser" test rather than the "first registered holder" test, a public corporation must elect under this new subsection by so indicating in the prescribed form that is required for purposes of the designation under subsection 192(4) of the Act. A special provision permits such a notification to be filed within 90 days following Royal Assent to the implementing legislation. This change is applicable after June 30, 1983.

ITA 127.2(11)

Concern has been expressed that some part of the consideration paid for a share carrying an entitlement to share-purchase tax credit may not be viewed as forming part of the cost of the share. Similarly, it is unclear that the consideration received

by the issuer for the share-purchase tax credit represents consideration received for the share. To eliminate any uncertainty, new subsection 127.2(11) stipulates that the consideration paid or received for any share-purchase tax credit is treated as part of the consideration for the share to which it pertains. In addition, the subsection stipulates that the consideration is not income to the issuer. These changes are applicable to the 1982 and subsequent taxation years.

Subclauses 43(4) to (6)

These set out the effective dates for the amendments to section 127.2 of the Act.

Scientific Research Tax Credit

Clause 44

Subclause 44(1)

ITA 127.3(2)(a)

Paragraph 127.3(2)(a) of the Act defines the scientific research tax credit of a taxpayer for a taxation year. The amendment to this paragraph corrects an error in the English version by adding the word "scientific" to that portion of the definition following subparagraph (v). This amendment applies to the 1982 and subsequent taxation years.

Subclause 44(2)

ITA 127.3(2)(b)

Paragraph 127.3(2)(b) of the Act defines the unused scientific research tax credit of a taxpayer for a taxation year. The amendment to this paragraph simplifies the definition and ensures that, as intended, the unused tax credit for a taxation year consists only of that portion of the credits acquired in that year that could not be utilized in the year. This change is applicable to the 1982 and subsequent taxation years.

Subclause 44(3)

ITA 127.3(3.1)

Subsection 127.3(3) of the Act permits a trust to allocate its scientific research tax credit to its beneficiaries. This flow-through mechanism is not intended to be available to trusts exempt from tax and trusts governed by an employee benefit plan or a revoked deferred profit sharing plan. Existing paragraph 146(2)(c.4) of the Act relating to registered retirement savings plans and analogous provisions dealing with other types of tax-exempt trusts may operate to trigger revocation of their exempt status in circumstances where such an allocation is made. This is because the allocation of scientific research tax credit can be viewed as a benefit conferred on the beneficiary that arises as a result of the existence of the trust.

New subsection 127.3(3.1) clarifies this matter by preventing these trusts from allocating credits. This restriction is necessary to prevent beneficiaries from withdrawing funds from such a trust in the form of credits on a tax-free basis. This change is applicable after the date on which the draft legislation was made public.

Subclause 44(4)

ITA 127.3(6)(b)

Subsection 127.3(6) of the Act provides rules for determining the cost to a taxpayer of a qualifying investment that has earned a scientific research tax credit. The amendment to paragraph 127.3(6)(b) includes a reference to a debt obligation or right. This amendment applies to the 1982 and subsequent taxation years.

Subclause 44(5)

ITA
127.3(9)

Under section 127.3 of the Act, only the first registered holder, other than a broker or dealer in securities, of a qualifying investment qualifies for a scientific research tax credit. In response to recent representations that this creates difficulties in the marketing of public issues of qualifying investments, new subsection 127.3(9) permits the first purchaser, other than a broker or dealer in securities, of a qualifying investment to qualify for the scientific research tax credit. To qualify under the "first purchaser" test rather than the "first registered holder" test, a corporation must elect under this new subsection by so indicating in the prescribed form that is required for purposes of the designation under subsection 194(4) of the Act. A special provision permits such a notification to be filed within 90 days following Royal Assent to the implementing legislation. This change is applicable after September, 1983.

ITA
127.3(10)

Concern has been expressed that some part of the consideration paid for a share, debt obligation or right carrying an entitlement to scientific research tax credit may not be viewed as forming part of the cost of the share, debt obligation or right,. Similarly, it is unclear that the consideration received by the issuer for the scientific research tax credit represents consideration received for the share, debt obligation or right. To eliminate any uncertainty, new subsection 127.3(10) stipulates that the consideration paid or received for any scientific research tax credit is treated as part of the consideration for the share, debt obligation or right to which it pertains. In addition, the subsection stipulates that the consideration is not income to the issuer. These changes are applicable to the 1982 and subsequent taxation years.

Subclauses 44(6) to (9)

These set out the effective dates for the amendments to section 127.3 of the Act.

Refundable Dividend Tax on Hand

Clause 45

Subclause 45(1)

ITA
129(3)(a)(iii)(B)

Subsection 129(3) of the Act defines the "refundable dividend tax on hand" of a private corporation. It represents that portion of the corporation's Part I tax on its net investment income which is refundable to the corporation on the payment of taxable dividends.

The repeal of clause 129(3)(a)(iii)(B) of the Act which refers to the amount deductible under subsection 125(1.1) is strictly consequential on the repeal of the concept of "non-qualifying business" described in the amendments to section 125. This amendment is applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation.

Subclauses 45(2) and (3)

ITA
129(4.1)
and (4.2)

Subsection 129(4) of the Act defines "Canadian investment income" and "foreign investment income" for the purposes of computing a private corporation's refundable dividend tax on hand. Subsection 129(4.1) provides that the income or loss of a corporation for the year from a source in Canada that is property includes the income or loss from a specified investment business carried on by it in Canada, other than income or loss from a source outside Canada, but does not include income from any other business or from property that is incident to, pertains to, or is used or held principally for the purpose of gaining income from an active business or a non-qualifying business carried on by it.

Subsection 129(4.2) provides that income or loss for the year from a source outside Canada that is property does not include the income or loss from any property that is incident to, pertains to, or is used or held principally for the purpose of gaining or producing income from an active business or non-qualifying business carried on by it.

The amendments to paragraphs 129(4.1)(b) and (c) and 129(4.2)(a) and (b) remove all references to a "non-qualifying business" and are strictly consequential on the repeal of the concept of "non-qualifying business" as part of the small business simplification measures. The amendments apply to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation.

Investment Income from Associated Corporation

Subclauses 45(4) and (5)

ITA
129(6)

Subsection 129(6) of the Act deems the property income of a corporation to be income from an active business or a non-qualifying business where it was received from an associated corporation and resulted in a deduction in computing the associated corporation's income from an active business or non-qualifying business.

The amendments to subparagraph 129(6)(a)(i) and 129(6)(b) serve to remove the references to a "non-qualifying business" and are strictly consequential on the

repeal of the concept of "non-qualifying business" as part of the small business simplification measures. The amendments are applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation.

Subclause 45(6)

New subsection 129(8) of the Act simply ensures that the section 125 definitions apply for the purposes of section 129.

Subclause 45(7)

This sets out the effective date for the amendments to section 129 of the Act.

Cooperative Corporations

ITA
136(1)

Clause 46

Subsection 136(1) of the Act deems a cooperative corporation not to be a private corporation except for the purposes of the corporate surtax and the small business deduction. The amendment to subsection 136(1), which is applicable for taxation years ending in calendar years commencing after Royal Assent to the implementing legislation, provides for two further exceptions. The first exception is for the purpose of determining the investment tax credit rate with respect to certain qualifying scientific research expenditures. The second exception is for the purpose of determining the refundable investment tax credit under section 127.1 of the Act. The effect of these amendments is to enable eligible cooperative corporations to obtain the benefit of the 35% rate of investment tax credit on qualifying scientific research expenditures and to obtain the right to a refund of 40% (instead of 20%) of any unused investment tax credit.

Clause 47

Subclause 47(1)

ITA
137(3)

Subsection 137(7) of the Act deems a credit union not to be a private corporation except for the purposes of the corporate surtax and the small business deduction. Subsection 137(3) provides that a corporation that was a credit union throughout a taxation year is permitted to deduct a further amount in computing its tax under Part I payable for the year so as to enable it to build an appropriate amount of reserve at the small business tax rate. Technically, the additional tax deduction is calculated at a rate 21% of the lesser of its taxable income not eligible for the small business deduction and the amount, if any, by which 4/3 of its maximum cumulative reserve at the end of the year exceeds its preferred rate amount at the end of its immediately preceding taxation year.

As part of the small business simplification measures, paragraph 125(1)(d) and the preferred-rate amount concept in Part VI of the Act are being repealed. As a consequence, the existing references in subsection 137(3) to paragraphs 125(1)(d) and 190(2)(b) of the Act are being removed. However, since the preferred-rate amount continues to be relevant for credit unions, a new subsection 137(4.3) is being introduced to define the "preferred rate amount" for a credit union and the amendments to subsection 137(3) pick up this new subsection 137(4.3) reference. This ensures that the basis for the additional reserve-related tax deduction is maintained.

Subclause 47(2)

ITA
137(4.3)

New subsection 137(4.3) of the Act defines "preferred rate amount" of a corporation at the end of a taxation year. The preferred rate amount is used in calculating a credit union's special reserve-related tax deduction under subsection 137(3) of the Act.

The addition of this subsection, applicable to taxation years ending in calendar years commencing after Royal Assent to this amendment, is strictly consequential on the repeal of paragraph 87(2)(ee) and section 190 and the amendments to paragraph 88(1)(e.2) dealing with the preferred rate amount arising as a result of the small business simplification measures.

New subsection 137(4.3) of the Act defines "preferred rate amount" of a corporation at the end of a taxation year to be the aggregate of its preferred rate amount at the end of its immediately preceding taxation year and 4 times the amount deductible from its tax otherwise payable for the year under section 125 of the Act. The definition also ensures that preferred rate amounts of predecessor corporations and subsidiaries, as the case may be, flows through to the new corporation or the parent, as the case may be, where there has been an amalgamation within the meaning assigned by subsection 87(1) or a winding-up of a wholly-owned subsidiary to which subsection 88(1) applied.

Subclause 47(3)

ITA 137(7)

Subsection 137(7) of the Act deems a credit union not to be a private corporation except for the purposes of the corporate surtax and the small business deduction.

The amendment to subsection 137(7), applicable for taxation years ending in calendar years commencing after Royal Assent to the implementing legislation, provides two further exceptions under which an incorporated credit union or caisse populaire will qualify as a private corporation. The first is for the purpose of determining the investment tax credit rate with respect to certain qualifying scientific research expenditures. The second exception is for the purpose of determining the refundable investment tax credit under section 127.1 of the Act. The effect of these amendments is to enable eligible credit unions and caisses populaires to obtain the benefit of the 35% investment tax credit rate on qualifying scientific research expenditures and to obtain the right to a refund of 40% (instead of 20%) of unused investment tax credits.

Subclause 47(4)

This sets out the effective date for the amendments to section 137 of the Act.

Registered Retirement Savings Plans

Clause 48

Section 146 of the Act deals with registered retirement savings plans. One set of amendments provides a special farm capital gain rollover while a second amendment addresses a spousal RRSP concern.

Subclause 48(1)

New subsections 146(5.3) to (5.5) are added to the Act to allow a taxpayer to defer the tax on up to $120,000 of taxable capital gains arising on the disposition of qualified farm property owned by him or his spouse on December 31, 1983. This tax deferral is achieved by allowing a special deductible contribution to a registered retirement savings plan or, where the taxpayer has passed the age limit for contributing to a registered retirement savings plan, the acquisition of a qualified annuity.

ITA 146(5.3)

New subsection 146(5.3) allows a taxpayer a deduction in computing his income for a year for amounts paid by him to a registered retirement savings plan in the year or within 60 days after the end of the year as a special contribution in respect of taxable capital gains from the disposition of a qualified farm property.

The maximum amount of the special contribution that may be made by a taxpayer for a taxation year cannot exceed the lesser of two amounts. The first is the aggregate of his taxable capital gains from all dispositions of qualified farm property after 1983. The second is the amount by which his "farm contribution limit" for the year exceeds the total of all contributions (other than special contributions) made by him to a registered retirement savings plan or registered pension plan for the 1984 and subsequent taxation years. The maximum amount of the special contribution for any year is further reduced by any special contributions made by him for preceding taxation years.

ITA 146(5.4)

New subsection 146(5.4) provides definitions for the purposes of new subsection 146(5.3).

ITA 146(5.4)(a)

Paragraph 146(5.4)(a) defines the expression "qualified farm property" of a taxpayer. To qualify as such, the property must in all cases have been owned by the taxpayer or his spouse on December 31, 1983. Property so owned will qualify if it is real property that was used in the business of farming at some time between 1972 and 1983 inclusive by the taxpayer, his spouse, any of his children or a farm corporation or partnership of his family. A share of the capital stock of a family farm corporation and an interest in a family farm partnership may also constitute qualified farm property. For this purpose, the expressions a "share of the capital stock of a family farm corporation" and "interest in a family farm partnership", have the meanings as set out in paragraphs 70(10)(b) and (c) of the Act.

ITA 146(5.4(b)

Paragraph 146(5.4)(b) defines the expression "farm contribution limit" for a year. A taxpayer's farm contribution limit is determined first by multiplying $10,000 by the number of calendar years after 1971 and before 1984 during which he or his spouse was a full-time farmer. Thus, a taxpayer who was a full-time farmer throughout that period would have a maximum farm contribution limit of $120,000. The farm contribution limit for a year is reduced by any special contributions

claimed under subsection 146(5.3) by the taxpayer's spouse for the year and preceding years.

ITA 146(5.4(c)

Paragraph 146(5.4)(c) defines the expression "full-time farmer". This expression is relevant in determining a taxpayer's contribution limit. A full-time farmer means an individual who owned a share of the capital stock of a family farm corporation or who leased land for use in the business of farming to his spouse, child, or family farm corporation or to a family farm corporation or partnership of his spouse or child. A full-time farmer also includes any individual who was actively engaged in the business of farming other than an individual who was or would, if he had losses, be subject to the restricted farm loss rules in section 31 of the Act.

Example

Assume that a taxpayer who was a full-time farmer from 1974 to 1983 inclusive retired from farming in 1984 at which time he rented his farmland to an unrelated party. In 1987 he sold the farmland, which was qualified farm property, and realized a taxable capital gain of $150,000. Assume further that the taxpayer made regular annual contributions of $2,000 to his registered retirement savings plan in 1984, 1985 and 1986 and that his spouse made a special contribution under subsection 146(5.3) in 1986 of $25,000.

The maximum amount that the taxpayer can deduct under subsection 146(5.3) as a special contribution to his registered retirement savings plan is the lesser of:

(i) his taxable capital gain from the disposition of a qualified farm property = $150,000

and

(ii) his farm contribution limit for the year of $75,000 ($100,000 less the $25,000 contribution made by his spouse in 1986) minus $6,000 (the total of his regular registered retirement savings plan contributions after 1983) = $ 69,000

Therefore the taxpayer's maximum special contribution for 1987 is $69,000.

ITA 146(5.5)

New subsection 146(5.5) provides that a taxpayer who is over the age limit for making contributions to a registered retirement savings plan may nevertheless take advantage of the special deduction allowed under new subsection 146(5.3). This subsection treats the cost to such a taxpayer of an annuity described in subparagraph 60(1)(ii) of the Act to be a premium paid under a registered retirement savings plan of which he is an annuitant. The cost of such an annuity will therefore qualify for the special deduction. A qualifying annuity for this purpose is a level-payment annuity under which payments commence within one year of its purchase and continue to the taxpayer for life or until he reaches 90 years of age.

These amendments relating to special contributions for farm capital gains apply to the 1984 and subsequent taxation years.

Subclause 48(2)

ITA 146(8.3)

A taxpayer may deduct contributions made, within certain limits, to his spouse's registered retirement savings plan. However, subsection 146(8.3) of the Act provides that any withdrawals made in a year from the spouse's plan (other than to acquire a life annuity on maturity of the plan) will be included in the taxpayer's income to the extent of the deductible contributions made by him to the plan in that year and the 2 immediately preceding years. This rule is essentially designed to prevent income-splitting between spouses since in its absence the RRSP contributions would be deductible to the taxpayer but taxable on withdrawal to his spouse. The rule is not appropriate in cases of a marriage breakdown and the amendment ensures that subsection 146(8.3) will not apply with respect to a withdrawal of funds from the plan if it is made after February 15, 1984 and at a time when the taxpayer and his spouse are living apart and separated as a result of the breakdown of their marriage and pursuant to a judicial separation or a written agreement.

Subclauses 48(3) and (4)

These set out the effective dates for the amendments to section 146 of the Act.

Registered Home Ownership Savings Plans

ITA
146.2(4)(i)

Clause 49

A beneficiary under a registered home ownership savings plan (RHOSP) is permitted a special "top-up" deduction in 1983 or 1984. This deduction is generally available where the beneficiary uses the funds in his plan in the year or within 60 days after the end of the year to acquire or build a new housing unit provided that neither he nor his spouse previously owned a dwelling after 1981, no other person claims a similar deduction in respect of the same housing unit and no grant is payable under the National Housing Act in respect of that housing unit. In order to qualify for the deduction, a qualifying individual who has never been a beneficiary under a RHOSP does not have to open a RHOSP to claim such a deduction. A technical amendment to paragraph 146.2(4)(i) denies an individual who wishes to claim the top-up deduction as a non-beneficiary of an RHOSP the right to open an RHOSP once he has acquired his new housing unit. The amendment to this paragraph also ensures that by making the election, the individual is not only deemed to have been a beneficiary under an RHOSP, but he is also deemed to have complied with the other requirements normally applicable to a beneficiary before the top-up deduction may be granted.

Deferred Profit Sharing Plans

ITA
147(2)(k.2)(ii)

Clause 50

Section 147 of the Act contains the provisions relating to deferred profit sharing plans. Subsection 147(2) sets out the conditions that must be met for a profit sharing plan to qualify for registration. One of these conditions, set out in subparagraph 147(2)(k.2)(ii), provides that principal shareholders or their relatives cannot be beneficiaries under the plan. The subparagraph refers to an individual who is, or is related to, a specified shareholder of the employer or of a corporation related to the employer. As part of the small business simplification measures, the definition of specified shareholder is being moved from paragraph 125(9)(c) of the Act to subsection 248(1) so that it applies for all purposes of the Act without the need for cross-references. The amendment to subparagraph 147(2)(k.2)(ii) is strictly consequential on this change and simply deletes the existing reference to paragraph 125(9)(c). The amendment is applicable to taxation years ending in calendar years that commence after Royal Assent to the implementing legislation.

Clause 51

ITA
149.1(1)

Section 149.1 of the Act deals with registered charities. It provides the rules that must be met for these charities to obtain and keep registered status. A registered charity is exempt from tax on its income and can issue receipts which entitle taxpayers to deduct donations in computing their taxable income.

Subclauses 51(1) to (19)

Subsection 149.1(1) of the Act contains the definitions that are relevant for the purposes of section 149.1. The amendment to the preamble of this subsection adds a reference to section 172 and new Part V to ensure that the definitions in section 149.1 apply for purposes of those provisions.

ITA
149.1(1)(b)

Paragraph 149.1(1)(b) of the Act currently defines a ''charitable organization'' as being an organization all of the resources of which are devoted to charitable activities carried on by it and no part of the income of which is available for the benefit of any member. For taxation years commencing after 1984, this definition is amended to require a charitable organization to have an independent board of directors or trustees. It provides that more than 50% of the directors, trustees, officers or other similar officials of a charitable organization must deal with each other and with each of the other directors, trustees or other similar officials at arm's length. A further amendment to this definition, applicable to taxation years commencing after 1984, requires a charity that applies for registration as a charitable organization after February 15, 1984, or a charity that had been previously designated as a private or public foundation, to comply with an additional requirement to be classified as a charitable organization: not more than 50% of its capital may have been contributed by a person or group of persons not dealing with each other at arm's length. Such a person would not include a government, a municipality, another registered charity that is not a private foundation or a non-profit organization described in paragraph 149(1)(l) of the Act.

ITA
149.1(1)(e)

Paragraph 149.1(1)(e) of the Act defines the ''disbursement quota'' of a private foundation. This definition is repealed and a new definition of ''disbursement quota'' for both private and public foundations is substituted. The disbursement quota is the amount that a charitable foundation is required to spend annually on charitable activities or as gifts to qualified donees. For taxation years commencing after 1983, this will be the aggregate of the following amounts:

1. 80% of all amounts it receives in its immediately preceding taxation year for which it issued receipts. Two types of receipted donations are excluded— those which are received out of the capital of a testamentary estate and those which are subject to a direction that they be retained by the charity for at least 10 years (subparagraph 149.1(1)(e)(i)).

2. If it is a private foundation, 100% of all amounts it receives in its immediately preceding taxation year from one or more other registered charities, or if it is a public foundation, 80% of all such amounts. Excluded from this requirement are ''specified gifts''. A ''specified gift'' is a gift from a registered charity that is designated as such by it in its information return and the amount of which is not included by the donor in computing the amount that it has expended on charitable activities or as gifts made by it to qualified donees.

3. 4.5% of the value of its investment assets at the beginning of the year. An investment asset of a foundation is any property or any portion thereof owned by it to the extent not used in charitable activities throughout the immediately preceding year. It is assumed that generally funds which are subject under subparagraph (i), (ii) and (iii) to the 80% and 100% requirements will be on hand and included in the charity's pool of investment assets at the beginning of the year following the year of receipt but will be spent during that following year. Accordingly, the amounts of such funds are subtracted from the value of investment assets on which the 4.5% rate is calculated.

For the first 10 years of application of this new disbursement quota system, a transitional rule is provided in subparagraph 149.1(1)(e)(v) for those foundations that claimed an income reserve under subsection 149.1(18) of the existing law for the last taxation year commencing before 1984. If the existing provisions were to continue in force, a foundation's disbursement quota would include, in its first taxation year commencing after 1983, 90% of any such reserve claimed in the previous year. The special transitional rule requires a minimum portion of that reserve to be included in the foundation's disbursement quota in each of the 10 years commencing after 1983.

ITA
149.1(1)(e.1)

Paragraph 149.1(1)(i) of the Act currently provides a definition of "qualified investment" for a private foundation. Where a private foundation holds an investment that is not a qualified investment, it is required to include 5% of the fair market value of such investment in determining its disbursement quota. For taxation years commencing after 1983, the definition of "qualified investment" is repealed. New paragraph 149.1(1)(e.1) defines a "non-qualified investment" as a debt instrument, share or right to acquire a share held by a private foundation that is issued by certain persons who are in a position to control or influence the operations of the foundation. New Part V of the Act provides for a tax to be imposed on the issuer of such an investment where it fails to produce the required minimum rate of return (see comments under Part V). Excluded from the definition of non-qualified investments are shares that are listed on a prescribed stock exchange, qualifying equity shares (similar to those defined in subsection 192(6) for purposes of the share purchase tax credit) and debts owing by or shares in a limited dividend housing company or a corporation whose sole purpose is to hold property to be used by a registered charity in its charitable activities or administration.

ITA
149.1(1)(g)

Paragraph 149.1(1)(g) of the Act defines a "public foundation" as a charitable foundation in respect of which more than 50% of the directors or trustees deal with each other and with each of the other directors or trustees at arm's length and not more than 75% of the capital of which has been contributed by a person or group of persons who do not deal with each other at arm's length. For taxation years commencing after 1983, this definition is slightly modified in respect of public foundations registered after February 15, 1984 or designated at any time as private foundations or charitable organizations. For those foundations, more than 50% of the directors, trustees, officers or other similar officials will be required to deal with each other at arm's length and the maximum amount of capital that may be contributed by one person or a group of non-arm's length persons will be reduced from 75% to 50%. Such a person will not include a government, a municipality, an agency thereof, another registered charity that is not a private foundation or a non-profit organization described in paragraph 149(1)(l) of the Act. A special transitional rule provides that in the first taxation year of a charity

commencing after 1983 the existing definition of "public foundation" will apply but with the exclusion relating to governments and others described above.

ITA 149.1(1)(i)

Paragraph 149.1(1)(i) of the Act defines "qualified investment" for a private foundation. For taxation years commencing after 1983, this definition is repealed and replaced by the concept of "non-qualified investment" found in new paragraph 149.1(1)(e.1).

ITA 149.1(1)(k)

Paragraph 149.1(1)(k) of the Act is a transitional rule relating to amendments made in 1976. It sets out an increasing scale of "relevant percentages" for the purpose of determining the amount that a charitable organization and public foundation are required to expend on charitable activities or as gifts to qualified donees. This percentage has been fixed at 80% since 1979. As it is no longer required, this paragraph is repealed for taxation years commencing after 1983.

New paragraph 149.1(1)(k) introduces the definition of "specified gift". A "specified gift" means a gift made by a registered charity to another registered charity that is designated by the donor charity in its information return for the year as a specified gift.

ITA 149(1.1)

New subsection 149(1.1) is added to ensure that a specified gift is not included in determining the amount that the donor charity has expended on charitable activities and as gifts to qualified donees.

A specified gift is not included in determining the disbursement requirements of the recipient charity, and will be used where the donor charity wants to make a gift to a charitable foundation in circumstances where it does not want that foundation to be required to spend 100% or 80% of the gift in the following year.

ITA 149.1(2)(b)

Subsection 149.1(2) of the Act sets out the reasons for which the Minister of National Revenue may revoke the registration of a charitable organization. Paragraph 149.1(2)(b) provides that such registration may be revoked where the organization fails to expend in a year on charitable activities or as gifts to qualified donees the relevant percentage of its receipted donations received in the previous year. The relevant percentage has been 80% in respect of receipted donations received in taxation years after 1978. For taxation years commencing after 1983, this paragraph is amended so that the registration of a charitable organization may be revoked where it fails to expend 80% of its receipted donations received in its previous year other than gifts received out of the capital of a testamentary trust and gifts which are subject to a direction that they be retained by the charity for at least 10 years.

ITA 149.1(3)(b)

Subsection 149.1(3) sets out the reasons for which the Minister of National Revenue may revoke the registration of a public foundation. Paragraph 149.1(3)(b) provides that such registration may be revoked for failure to expend the required amount on charitable activities or as gifts to qualified donees. For taxation years commencing after 1983, this required amount is the disbursement quota of the foundation as defined in paragraph 149.1(1)(e).

ITA 149.1(4.1)

New subsection 149.1(4.1) is added to authorize the Minister of National Revenue to revoke the registration of a registered charity that has made a gift to another registered charity where the Minister is satisfied that one of the main reasons for making the gift was to unduly delay the expenditure of amounts on charitable

activities. The Minister may also revoke the registration of the recipient charity where it co-operated with the donor charity to achieve the delay. Thus, for example, where a group of charities merely circulates funds among the members of the group rather than expending them on charitable activities, their registrations can be revoked.

ITA
149.1(5)

Subsection 149.1(5) currently provides that the Minister of National Revenue shall not revoke the registration of a charitable organization or public foundation in a year in which it fails to meet certain of its disbursement requirements if the aggregate of amounts it expended on charitable activities or as gifts to qualified donees in the year and the 4 immediately preceding years is at least equal to 80% of the amount for which it issued receipts in the 5 immediately preceding years. For the 1984 and subsequent taxation years, this subsection is repealed and replaced by a provision which authorizes the Minister of National Revenue, upon application by a registered charity, to reduce the disbursement requirements of that charity for a particular year. This provision could, for example, apply to a year in which a charity fails to meet its disbursement requirements due to excessive start-up costs or an unsuccessful fund-raising campaign. It is intended that the Minister will exercise his discretion under this subsection where the applicant charity cannot fully correct the deficiency by applying disbursement excesses from other years pursuant to subsection 149.1(20). It is also intended to be used where a charity has made disbursements prior to 1984 that could have been included under the averaging mechanism provided in the former subsection 149.1(5).

ITA
149.1(9)

Subsection 149.1(8) of the Act currently allows a charity that obtains Ministerial approval to accumulate funds for a particular purpose. Funds so accumulated by a charity in any particular year are deemed to have been expended in that year on charitable activities carried on by the charity. Subsection 149.1(9) of the Act provides that where property that has been so accumulated is not used for the purpose for which it was accumulated, such property shall be deemed to be income of the charity for the year in which the charity fails to or decides not to use the property for the intended purpose and, accordingly, only affects the disbursement quota of charitable foundations. For taxation years commencing after 1983, this subsection is amended to provide that accumulated property which a charity fails to or decides not to use for its intended purpose will also be deemed to be a receipted donation of the charity. This amendment is necessary in order to ensure that the property is brought into the disbursement quota of all registered charities and actually disbursed in the following year.

ITA
149.1(11)

Subsection 149.1(11) of the Act currently provides that capital gains and losses not be taken into account in calculating the income of a charitable foundation upon which its disbursement requirements are based. For taxation years commencing after 1983, there will no longer be any provisions that require such a calculation for this purpose and, accordingly, subsection 149.1(11) is repealed.

ITA
149.1(12)(a)

Paragraph 149.1(12)(a) of the Act sets out the circumstances in which a charitable foundation is deemed to control a corporation for the purposes of the provisions relating to the deregistration of public foundations and private foundations in paragraphs 149.1(3)(c) and (4)(c) respectively. It provides that a foundation will be deemed not to have acquired control of a corporation for this purpose if it has not purchased or acquired for consideration any of the shares of the corporation. For taxation years commencing after 1983, this paragraph is amended to provide

that a foundation will be deemed not to have acquired control of a corporation if it has not purchased or otherwise acquired for consideration more than 5 per cent of the issued shares of any class of the corporation's shares.

ITA 149.1(12)(b)

Paragraph 149.1(12)(b) of the Act sets out the rules relating to the computation of income of a charity. These rules are generally relevant for the purpose of determining the extent to which gifts can be made by charitable organizations to qualified donees. Generally, the income of a charity includes all gifts it receives in the year. There are, however, several significant exclusions such as 10 year endowments and gifts from another charity that are made out of capital. For taxation years commencing after 1983, subparagraph 149.1(12)(b)(i) is amended to add to the list of exclusions gifts made out of the capital of a testamentary trust and specified gifts as defined in paragraph 149.1(1)(k).

ITA 149.1(14)

Subsection 149.1(14) of the Act requires that each registered charity file an information return and a public information return within 3 months from the end of its taxation year. For the 1984 and subsequent taxation years, this subsection is amended to extend the time within which such returns must be filed to 6 months after the end of the charity's taxation year.

ITA 149.1(16)

Subsection 149.1(16) of the Act applies a special tax following the revocation of a charity's registration where all its assets are not transferred to other registered charities. For taxations years commencing after 1983, this subsection is repealed and such tax will be imposed under subsection 188(1) in new Part V of the Act.

ITA 149.1(17)

Subsection 149.1(17) of the Act imposes a tax liability, jointly with a deregistered charity, on persons, other than qualified donees, who receive property of the charity where its registration has been revoked. For taxation years commencing after 1983, this subsection is repealed and such joint liability will be imposed under subsection 188(2) in new Part V of the Act.

ITA 149.1(18)

Subsection 149.1(18) of the Act currently allows a charitable foundation to establish an income reserve for a taxation year and requires the inclusion of that reserve in income in the following year. For taxation years commencing after 1983, an income reserve is not required as the disbursement test is no longer based on income. The subsection is, accordingly, repealed. There will be a transitional rule in subparagraph 149.1(1)(e)(v) of the definition of "disbursement quota" to allow any remaining reserve to be used up over a period of up to 10 years.

ITA 149.1(20)

Subsection 149.1(20) of the Act allows a registered charity, with prior written approval by the Minister of National Revenue, to expend a disbursement excess (as defined in subsection 149.1(21)) in a year and to include that excess in the computation of amounts expended on charitable activities and as gifts to qualified donees for up to 3 taxation years following that year. For the 1984 and subsequent taxation years, this subsection is amended to allow a registered charity to include a disbursement excess for a year in computing the amount it has expended on charitable activities or as gifts to qualified donees for the immediately preceding and up to 5 subsequent taxation years. Further, it will no longer be necessary to obtain prior Ministerial approval.

ITA 149.1(21)

Subsection 149.1(21) of the Act defines "disbursement " for the purposes of subsection 149.1(20). For the 1984 and subsequent taxation years, this definition is amended as a consequence of the modification to the disbursement requirements

of charitable foundations and organizations. The disbursement excess is the amount by which a registered charity's expenditures in the year exceeds its disbursement requirements for the year.

Subclauses 51(20) to (23)

These set out the effective dates for the changes to section 149.1, which generally are applicable to taxation years commencing after 1983.

Tax Returns

ITA
150(1)

Clause 52

Section 150 of the Act sets out the requirements relating to the filing of tax returns. Subsection 150(1) stipulates when the different categories of taxpayers must file returns. Two amendments are being made to this subsection. First, for taxation years commencing after 1983, subsection 150(1) is amended to remove corporations that are registered charities from the scope of this section since such corporations will not be subject to tax under Part I. The filing requirement for such corporations is provided in subsection 149.1(14) which requires the information and public information returns for a registered charity to be filed within six months from its year-end.

The second amendment to the subsection relates to the obligation of an individual to file a tax return. Under the existing provision an individual is required to file a return only for those years for which tax is payable. Subsection 150(1) is amended to require an individual to file a return for a year for which tax would have been payable by him but for the fact that he claimed a share-purchase or scientific research tax credit under sections 127.2 or 127.3 of the Act. This amendment, applicable to the 1983 and subsequent taxation years, ensures that a tax return is filed in such circumstances in order to determine the amount of any interest on deficient tax instalments for the year.

Clause 53

Subclause 53(1)

ITA
152(4.1)

Subsection 152(4) of the Act provides that in the absence of fraud or misrepresentation the Minister of National Revenue generally may not reassess tax after four years from the date of mailing of the original notice of assessment unless the taxpayer has filed a waiver within the 4-year period. Typically, a taxpayer may wish to file a waiver in order to permit the Minister to issue a favourable reassessment for a statute-barred year or to provide more time in which to resolve a matter in dispute before a reassessment is made. Under the existing Act, the filing of a waiver leaves the matter in respect of which the waiver was furnished open for reassessment indefinitely. New subsection 152(4.1) provides that a taxpayer may upon six month's notice revoke a waiver so that no further assessment may be made under its authority. This amendment applies to permit notices of revocation to be filed after February 15, 1984 in respect of waivers filed at any time under section 152.

Subclause 53(2)

ITA
152(6)

Subsection 152(6) of the Act provides for the reassessment of a taxpayer's tax for a year where the taxpayer has filed a prescribed form claiming an amount to be carried back from a subsequent taxation year such as a loss carryover or an investment tax credit. The amendment to this provision is consequential on the introduction of the 3-year carryback for foreign tax credits under section 126 of the Act. The amendment which is applicable to the 1984 and subsequent taxation years, requires the Minister of National Revenue to reassess preceding taxation years in order to give effect to the taxpayer's carryback of unused foreign tax credits.

Subclauses 53(3) and (4)

These set out the effective dates for the amendments to section 152 of the Act and provide an extension of the time for filing the prescribed form required to carryback an unused foreign tax credit.

Tax Instalments of Farmers and Fishermen

ITA
155(1)(a)(i)

Clause 54

Subparagraph 155(1)(a)(i) of the Act allows a person whose chief source of income is farming or fishing to pay a single tax instalment on December 31 of each year of 2/3 of his estimated tax payable for the year or of his instalment base for the preceding year. Subparagraph 155(1)(a)(i) is amended to provide that the instalment is based on tax payable before deducting the share purchase and scientific research tax credits allowed under sections 127.2 and 127.3 of the Act. This amendment generally applies to tax credits earned after February 15, 1984, subject to a special transitional rule for credits earned before March 1, 1984.

Tax Instalments of Individuals

ITA
156(1)(a)(i)

Clause 55

Subparagraph 156(1)(a)(i) of the Act requires certain individuals, other than farmers or fishermen, to pay quarterly tax instalments based on the lesser of their estimated tax payable for the year and their instalment base for the preceding year. Subparagraph 156(1)(a)(i) is amended to provide that such instalments are based on the tax payable before deducting the share purchase and scientific research tax credits allowed under sections 127.2 and 127.3 of the Act. This amendment generally applies to tax credits earned after February 15, 1984, subject to a special transitional rule for credits earned before March 1, 1984.

Instalment Requirements For Individuals
ITA
156.1

Clause 56

Section 156.1 of the existing Act exempts an individual from the requirement to pay tax instalments during a taxation year if his federal tax payable for the year or the preceding year is $400 or less. This amendment generally increases the threshold amount to $1000. A special rule for Québec taxpayers ensures that their tax payable for this purpose is offset by the amount that is treated under subsection 120(2) of the Act as having been paid on account of tax for the year. These changes are applicable to the 1984 and subsequent taxation years. In addition, the amendment requires the threshold tax payable to be determined before deducting any share-purchase or scientific research tax credit claimed by the individual. These special credits are provided for in sections 127.2 and 127.3 of the Act.

Instalment Requirements for Corporations

Clause 57

Subclause 57(1)

ITA
157(1)(a)(i)

Subparagraph 157(1)(a)(i) of the Act generally requires corporations to pay monthly tax instalments. This subparagraph is amended to provide that the amount of a corporation's tax instalments are to be determined on the basis of its estimated tax payable before deducting the share-purchase and scientific research tax credits allowed under sections 127.2 and 127.3 of the Act. This amendment does not restrict a corporation's ability to deduct these special credits in calculating the final payment of tax required under paragraph 157(1)(b). This amendment generally applies to tax credits earned after February 15, 1984, subject to a special transitional rule for credits earned before March 1, 1984.

Subclause 57(2)

ITA
157(1)(b)(i)

Subsection 157(1) of the Act specifies the time for payment of a corporation's taxes for a taxation year. A corporation must pay tax instalments at the end of each month during its taxation year and the balance of the tax payable by it for the year must be paid on or before the last day of the second month following its year or, where the corporation is a Canadian-controlled private corporation that has claimed a small business deduction, on or before the last day of the third month following its year end.

The amendment to subparagraph 157(1)(b)(i) is consequential on the amendments to section 125 relating to the small business deduction. It affects any corporation that was throughout the year, a Canadian-controlled private corporation provided that the aggregate of its taxable income for the year and the taxable income of all other corporations with which it was associated does not exceed the total of their business limits for those years. In these circumstances the corporation is entitled to pay the balance of its tax payable for a year on the last day of the third month following its year-end. For other corporations, the balance of tax owing must be paid by the last day of the second month following its year end.

This amendment is applicable to taxation years ending in calendar years following that in which Royal Assent is given the implementing legislation.

Subclause 57(3)

ITA
157(2.1)

Under subsection 157(1) of the Act, corporations are generally required to pay monthly tax instalments. New subsection 157(2.1) exempts a corporation from the requirement to pay instalments for a year where its taxes payable (computed without reference to any share-purchase or scientific research tax credits to which it is entitled) or first instalment base for the year is $1,000 or less. In these circumstances, the corporation will be required to pay its full tax by the end of the second month after the end of its taxation or, in the case of a company whose taxable income for the year does not exceed its business limit, by the end of the third

month after its year-end. This change is applicable to the 1984 and subsequent taxations years.

Subclauses 57(4) to (6)

These set out the effective dates for the amendments to section 157 of the Act.

Joint and Several Liability

ITA
160(4)

Clause 58

For tax purposes any income, gains or losses arising from property transferred between married individuals is attributable to the spouse who transferred the property. Subsection 160(1) of the Act provides, however, that both spouses are liable for any tax arising from the attributed amounts. In addition where a taxpayer transfers property to his spouse for consideration which is less than its fair market value, subsection 160(1) provides that the spouse is jointly and severally liable for taxes payable by the taxpayer for the year of the transfer and preceding years to the extent that the fair market value of the transferred property exceeds the amount of consideration received.

New subsection 160(4) ensures that the provisions of subsection 160(1) will not apply in respect of property transferred after February 15, 1984 by a taxpayer to his spouse pursuant to a court order or a written separation agreement if, at the time the property was transferred, the taxpayer and the spouse were separated and living apart as a result of the breakdown of their marriage. In addition, in respect of a transfer of property that meets these conditions but that was made before February 16, 1984, the new subsection discharges on February 16, 1984 any amount then owing by the spouse under subsection 160(1) with respect to the transferred property.

Interest on Deficient Tax Instalments

Clause 59

Subclause 59(1)

ITA 161(2.1)

Subsection 161(2) of the Act requires taxpayers to pay interest on late and deficient tax instalments for a year. New subsection 161(2.1) eliminates the obligation to pay such interest where the interest liability in respect of both the federal and provincial instalment payments for the year is $25 or less. This change is applicable to the 1984 and subsequent years.

ITA 161(4)(a) and (c)

Subsection 161(4) of the Act limits the interest charged on deficient instalments by an individual to the interest on the instalments that were not but that should have been paid based on his actual tax payable for the year. The amendments to paragraphs 161(4)(a) and (c) provide that the interest calculation will be based on the individual's actual tax for the year before deducting share-purchase and scientific research tax credits allowed under sections 127.2 and 127.3 of the Act.

Subclause 59(4)

ITA 161(4.1)

Subsection 161(4.1) of the Act limits the interest charged on deficient instalments by a corporation, to the interest on the instalments that were not but that should have been paid based on its actual tax payable for the year. The amendment to paragraph 161(4.1)(a) provides that the interest calculation will be based on the corporation's actual tax for the year before deducting share-purchase and scientific research tax credits allowed under sections 127.2 and 127.3 of the Act.

The amendments to subsections 161(4) and (4.1) generally apply to tax credits earned after February 15, 1984, subject to a special transitional rule for credits earned before March 1, 1984.

Subclause 59(5)

ITA 161(7)(a)(iv.1)

Under existing subsection 161(7) of the Act, where tax payable for a year is reduced as a consequence of the carryback of an amount from a subsequent year, the interest owing on any unpaid tax is calculated without regard to the reduction of tax for the period ending on the later of the day on which the tax return for the subsequent year is required to be filed and the day on which the return is actually filed. The amendment to paragraph 161(7)(a), which is consequential on the introduction of the 3-year carryback for foreign tax credits under section 126 of the Act, will extend the application of this provision to the calculation of interest owing on unpaid tax for a year where the tax liability is reduced as a result of the carryback of an unused foreign tax credit from a subsequent taxation year. The amendment to paragraph 161(7)(a) is applicable to the 1984 and subsequent taxation years.

Subclause 59(6)

ITA
161(10)

New subsection 161(10) is added to the Act as a consequence of the amendments to the tax instalment provisions which require the amount of instalments of tax payable during a year to be calculated without reference to any share-purchase and scientific research tax credits claimed by the taxpayer under sections 127.2 and 127.3 of the Act. The new subsection affects the calculation of interest on late or deficient tax instalments by treating these credits as a payment on account of tax made on the last day of the taxation year in which the credits were earned in any case where the taxpayer files his tax return for the year on time. If the return is filed late, the credits are considered to have been paid on the date the return is filed. This amendment applies to the 1983 and subsequent taxation years.

Subclauses 59(7) to (9)

These set out the effective dates for the amendments to section 161 of the Act.

Clause 60

Subclause 60(1)

ITA
164(4.1)

A taxpayer is entitled to a refund of tax resulting from his successful appeal of an assessment where the court has varied or vacated the assessment or the Minister of National Revenue has issued a reassessment. New subsection 164(4.1) of the Act provides that where on the disposition of an appeal a court has ordered the Minister to reassess, he shall with all due dispatch make the reassessment and refund any resulting overpayment, notwithstanding his intention to appeal the decision of the court. For greater certainty the amendment provides that the Minister's right to appeal the decision of the court will not be prejudiced by the issuance of the reassessment. This amendment is applicable after February 15, 1984.

Subclause 60(2)

ITA
164(5)(d.1)

Existing subsection 164(5) of the Act provides that to the extent that an overpayment of tax for a year results from the carryback of an amount from a subsequent year, such as a loss carryover or an investment tax credit, the interest payable to the taxpayer on the overpayment is calculated for the period commencing on the later of the day on which the tax return for the subsequent year is required to be filed and the day on which the return is actually filed. The amendment to subsection 164(5), which is consequential on the introduction of the 3-year carryback for foreign tax credits under section 126 of the Act, extends the application of this provision to the calculation of interest owing on an overpayment of tax resulting from the carryback of an unused foreign tax credit of a subsequent taxation year. This amendment is applicable to the 1984 and subsequent taxation years.

Subclauses 60(3) and (4)

These set out the effective dates for the amendments to section 164 of the Act.

Notice of Objection

ITA
165(1)

Clause 61

An assessment of tax under the Act is considered to be valid and binding until varied or vacated on an objection or appeal. In order to preserve his rights of objection and appeal, a taxpayer is currently required under subsection 165(1) of the Act to file a notice of objection with Revenue Canada, Taxation within 90 days of the date on which the disputed assessment was mailed to him. This amendment extends the objection period to 180 days for objections to assessments mailed after Royal Assent to the enacting legislation.

Revocation of Registration

ITA
168(2)

Clause 62

Section 168 of the Act deals with the revocation of the registration of registered charities. For taxation years commencing after 1983, subsection 168(2) is amended to replace the references to ''organization'' with references to ''charity''. This change ensures that the subsection is applicable to charitable foundations as well as charitable organizations.

Tax Court of Canada

Clause 63

Section 171 of the Act provides the rules applicable to income tax appeals disposed of by the Tax Court of Canada. Two amendments are being made to this section.

ITA 171(2)

Subsection 171(2) provides that the Tax Court of Canada has no jurisdiction to vacate or vary an assessment made in accordance with a direction of the Treasury Board under section 246 of the Act. An amendment is being made to repeal subsection 171(2) as a consequence of the repeal of section 246.

ITA 171(3)

Subsection 171(3) of the Act denies the Tax Court of Canada the authority to award costs on the disposition of an appeal. This provision is repealed and an amendment to section 18 of the Tax Court of Canada Act will be introduced to empower the Court to award a taxpayer his costs of an appeal.

The repeal of these two subsections is applicable with respect to appeals disposed of after the day on which the enacting legislation receives Royal Assent.

Appeal by Registered Charity

Clause 64

Subclauses 64(1) and (2)

ITA 172(3)

Subsection 172(3) of the Act provides a taxpayer with a right of appeal to the Federal Court of Appeal where it has applied for registration as a charity and the Minister of National Revenue refuses to so register it. Paragraph 172(3)(a) is amended to provide this appeal right where the Minister refuses to register an applicant that has applied for registration after February 15, 1984 as a charitable organization, public foundation or private foundation. This amendment is consequential to the amendment to the definition of "registered charity" in paragraph 110(8)(c).

172(3)(a.1)

Subsection 172(3) is further amended by the addition of new paragraph 172(3)(a.1), to provide a registered charity with a right of appeal where the Minister of National Revenue designates it or refuses an application for designation under subsection 110(8.1) or (8.2) after February 15, 1984.

Subclause 64(3)

ITA 172(4)(a)

Subsection 172(4) deems the Minister of National Revenue to have refused to register an applicant with 180 days of the filing of the application. Such an applicant would then have a right of appeal as provided by subsection 172(3). For applications for registration made after February 15, 1984, paragraph 172(4)(a) is amended to refer to registration as a charitable organization, private foundation or public foundation. This amendment is consequential to the amendment of the definition of "registered charity" in paragraph 110(8)(c).

ITA 172(4)(a.1)

Subsection 172(4) is further amended, in respect of applications for designation made after February 15, 1984, by the addition of paragraph 172(4)(a.1) which refers to an application for designation under new subsection 110(8.2).

Subclause 64(4)

ITA 172(4)

The amendment to the closing words of subsection 172(4) is strictly consequential on the addition of new paragraph 172(4)(a.1). By deleting the phrase "for registration or for the certificate, as the case may be", an application for designation by a registered charity will also be subject to the deemed refusal provisions of this subsection.

Subclause 64(5)

This sets out the effective date for the amendments to section 172 of the Act.

Costs in Federal Court of Canada

ITA
178(2)(a) and (b)

Clause 65

Subsection 178(2) of the Act requires the Federal Court of Canada to award a taxpayer his reasonable and proper costs of an appeal instituted by Revenue Canada if the amount of tax in dispute is not more than $2,500 or the amount of a disputed loss is not more than $5,000. This amendment increases these dollar limits. It provides that a taxpayer will be entitled to costs under subsection 178(2) where the tax or loss in controversy does not exceed $10,000 or $20,000 respectively. This amendment applies to appeals disposed of after Royal Assent to the enacting legislation.

Preferred Earnings Amount

ITA
181(2)(b)

Clause 66

Subsection 181(2) of the Act defines the term "preferred earnings amount" of a corporation at the end of any taxation year for the purposes of the corporate distributions tax under Part II of the Act. The amendment to paragraph 181(2)(b), which is applicable to taxation years ending in calendar years following that in which Royal Assent is given the implementing legislation, simply deletes the reference therein to paragraphs 125(1)(a) to (d) and substitutes therefor a reference to paragraphs 125(1)(a) to (c). This change is strictly consequential on the amendments to section 125 of the Act relating to the small business deduction.

Clause 67

Subclause 67(1)

ITA
186(1)(b.1)

Section 186 imposes a special tax, generally referred to as the Part IV tax, on dividends received by private and certain non-private corporations. Paragraph 186(1)(b.1) of the Act permits a corporation to elect to pay the Part IV tax on certain taxable dividends received by it and in respect of which the tax would not normally be required to be paid. Since taxable dividends received by a corporation free of the Part IV tax are added to its cumulative deduction account, the corporation may elect to pay tax under this provision in order to maintain its eligibility for the small business deduction which under existing section 125 is no longer available to a corporation when its cumulative deduction account exceeds $1 million. With the elimination of the cumulative deduction account paragraph 186(1)(b.1) is no longer required. The repeal of paragraph 186(1)(b.1) is applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation.

Subclause 67(2)

ITA
186(3)

Subsection 186(3) defines "dividend refund" and "cumulative deduction account" for the purposes of Part IV of the Act. The amendment to this subsection, applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation, simply deletes the reference to "cumulative deduction account" and is strictly consequential on the repeal of that concept as part of the small business simplification measures.

Subclause 67(3)

This sets out the effective date for the amendments to section 186 of the Act.

Tax in Respect of Registered Charities

Clause 68

ITA
Part V

New Part V of the Act has been added to provide for special taxes to be paid in connection with registered charities in particular circumstances. The tax relating to the revocation of a charity's registration has been moved from section 149.1 of the Act to new subsections 188(1) and (2). New subsection 188(3) imposes a special tax in certain situations where a charitable foundation transfers more than 50 per cent of its capital to a charitable organization, and new subsection 189(1) imposes a separate tax in respect of the non-qualified investments of a private foundation.

These changes are all applicable to taxation years commencing after 1983.

Revocation Tax

ITA
188(1)

Subsection 149.1(16) of the Act currently applies a special tax following the revocation of a charity's registration. For taxation years commencing after 1983, that subsection is repealed and the tax on revocation is imposed under new subsection 188(1). Under this provision a charity whose registration is revoked is required to pay a tax equal to the aggregate value of the assets of the charity on the day notice of revocation is mailed and the amount of receipted donations and inter-charity gifts received by the charity after that day. The amount of such tax will be reduced to the extent that assets or funds of the charity are transferred to other registered charities, used to repay its debts or used to cover its normal expenses in the period from the date the notice is mailed to one year from the date on which the revocation is effective.

ITA
188(2)

Subsection 149.1(17) of the Act currently imposes a tax liability, jointly with a deregistered charity, on persons, other than qualified donees, who receive property of the charity where registration has been revoked. For taxation years commencing after 1983, this joint liability is imposed under new subsection 188(2). The existing provision is altered to reduce any such liability to the extent the recipient of property has given consideration to the charity for it.

Tax on Transfer of Property

ITA
188(3)

New subsection 188(3) of the Act applies for taxation years commencing after 1983 where a charitable foundation transfers, to one or more charitable organizations in one or more transactions, property having a net value greater than 50 per cent of the net value of the foundation's assets and the main purpose of the transfer is to reduce its disbursement quota. In such a circumstance the foundation will be liable to pay a tax of 25 per cent of the net value of the property so transferred. This provision is intended to prevent a foundation from transferring property for the purpose of avoiding the application of the provision which increases its disbursement quota by 4.5 per cent of its investment assets.

ITA
188(4)

New subsection 188(4) of the Act imposes a tax liability commencing after 1983, jointly with a charitable foundation to which subsection 188(3) applies, on a charitable organization that has received property as referred to therein where the organization acted in concert with the foundation in attempting to reduce the foundation's disbursement quota. The liability of any particular organization is limited to the net value of the property it received from the foundation.

ITA 188(5)

New subsection 188(5) of the Act provides definitions of "net asset amount" and "net value" for the purposes of subsections 188(3) and (4). The "net asset amount" of a foundation means the fair market value of the foundation's assets less its liabilities. The "net value" of property transferred by a foundation is the fair market value of the property less the amount of any consideration given to the foundation for its transfer.

Tax on Non-Qualified Investment

ITA 189(1)

New subsection 189(1) of the Act imposes a tax, for taxation years commencing after 1983, on a taxpayer who is indebted to a private foundation in respect of a non-qualified investment of the foundation. The expression "non-qualified investment" is defined in new paragraph 149.1(1)(e.1) and, generally, means a share (other than a common share) or a debt held by a foundation that is issued by certain persons who are in a position to control or influence the foundation. The purpose of this tax, which also applies in respect of shares that are non-qualified investments by virtue of new subsection 189(3), is to ensure that taxpayers who issue debt or shares of this type to a foundation do not obtain the use of the foundation's funds without paying a reasonable rate of return thereon. This is achieved by imposing the tax on such a taxpayer where he has paid less than a required amount of interest or dividend to the foundation on a non-qualified investment. The tax is equal to the difference between the interest or dividend actually paid to the foundation on the investment and the interest (or two-thirds of the amount thereof in the case of a share) that would be payable based on applicable prescribed rates. Accordingly, no tax will be payable where the rate of return paid on the investment is comparable to the reference rate calculated according to the prescribed rates of interest that are in effect while the investment is outstanding. The prescribed rate is the rate of interest that is charged on tax deficiencies and paid on tax refunds. At the present time this rate is 10%. Employee loans to which the rules in subsection 80.4(1) and (3) apply are excluded from the application of this provision.

ITA 189(2)

For the purpose of determining whether the tax under subsection 189(1) is payable in respect of a non-qualified investment that is a debt, interest is to be calculated at such prescribed rates as are in effect during the period in a year that the debt was outstanding. A transitional rule is provided in new subsection 189(2) where the debt was incurred before April 22, 1982. For such a debt, the applicable rate of interest is the lesser of

- the prescribed rates in effect from time to time

and

- the rate of six per cent per annum increasing two percentage points for 1983 and every year thereafter.

April 21, 1982 is the date on which the rules regarding the minimum return on non-qualified investments were first announced and is, therefore, the transitional date for these investments.

ITA 189(3)

New subsection 189(3) of the Act deals with shares or rights to acquire shares held by a private foundation that are non-qualified investments. For purposes of the imposition of tax under subsection 189(1), such shares or rights are treated as

if they were debts having a face value equal to, in the case of shares or rights acquired before April 22, 1982, the greater of the fair market value of the shares or rights on April 21, 1982 and their cost amount to the foundation. In the case of shares or rights acquired after April 21, 1982, when the new rules relating to non-qualified investments were first announced, the value is their cost amount to the foundation. Tax under subsection 189(1) is equal to the difference between the amount of dividends actually paid and the amount determined by reference to two-thirds of the prescribed rates in effect from time to time while the shares or rights were held.

ITA 189(4)

New subsection 189(4) of the Act sets out a transitional rule for shares or rights acquired before April 22, 1982 for the purposes of the computation of the tax imposed under subsection 189(1). For such a share or right, the applicable rate of interest is the lesser of

- two-thirds of prescribed rates in effect from time to time

and

- a rate of four per cent per annum increasing one percentage point in 1988 and every five years thereafter.

ITA 189(5)

New subsection 189(5) of the Act ensures that a share or right that is substituted for a share or right originally acquired before April 22, 1982, will continue to be subject to the transitional rule in subsection 189(4). To qualify the substitution must be the result of a transaction to which section 51, 85, 85.1 86 or 87 of the Act applied.

ITA 189(6)

New subsection 189(6) of the Act requires a taxpayer who is liable for any tax under Part V to file a return, without notice or demand, and to estimate and pay the tax due. A taxpayer who is also liable under Part I must file the Part V return on or before the day his return under Part I is due. A registered charity or charity whose registration has been revoked must file this special return on or before the day that an information return is or would be required.

ITA 189(7)

New subsection 189(7) of the Act provides for the application for the purposes of Part V of certain of the provisions of Part I of the Act relating to the filing of returns, assessments, interest, penalties, objections and appeals.

Part VI Tax

ITA
190 and 191

Clause 69

Sections 190 and 191 of the Act constitute the Part VI of the Act. This Part levies a special tax where a corporation that was a Canadian-controlled private corporation that had previously claimed the small business deduction becomes controlled by persons not resident in Canada. This special tax is eliminated as a part of the measures proposed to simplify the rules of the Act relating to small business.

The repeal of these provisions is effective for taxation years ending in calendar years commencing after Royal Assent to the implementing legislation.

Part VII Tax – Late Designation

ITA
192(8)

Clause 70

Section 192 of the Act permits a corporation to flow out its investment tax credit on an issue of shares. Shareholders acquiring qualifying shares are entitled to obtain the benefit of this flow through in the form of a share-purchase tax credit for the amount designated by the issuing corporation. The designation is ordinarily required to be filed by the end of the month following that in which the qualifying share is issued. However, subsection 192(8) permits late-filed designations. The amendment to this subsection simply clarifies that the penalty for the late filing of the designation is required to be paid at the same time as the required prescribed form is filed. This change is applicable after June 1983.

Part VII Tax on Excess Designation

ITA
193(7.1)

Clause 71

New subsection 193(7.1) is added to the Act consequential to the introduction of new subsection 127.2(10). Subsection 127.2(10) allows a corporation that has made a public distribution of shares that carry a share-purchase tax credit to elect to have the credit apply to the first purchaser as opposed to the first registered holder (other than brokers or dealers in securities). As a consequence of this election, various persons involved in the distribution to the public of the shares will be required to file information returns to substantiate the credit claimed by the first purchasers. New subsection 193(7.1) provides for an amount of Part VII tax to be paid by such a person as a penalty where the total credits on information returns issued by him exceed the total credits available for distribution by him. The tax will be equal to the excess credits.

This amendment is applicable after June, 1983.

Part VIII Tax – Late Designation

ITA
194(7)

Clause 72

Section 194 of the Act permits a corporation to flow out the tax benefits of its scientific research expenditures on an issue of shares or debt obligations or granting of a right to income under a scientific research financing contract. Taxpayers acquiring a qualifying investment are entitled to obtain the benefit of this flow through in the form of a scientific research tax credit for 50% of the amount designated by the issuing corporation. The designation is ordinarily required to be filed by the end of the month following that in which the qualifying investment is issued or granted. However, subsection 194(7) permits late-filed designations. The amendment to this subsection simply clarifies that the penalty for the late filing of the designation is required to be paid at the same time as the required prescribed form is filed. This change is applicable after September 1983.

Part VIII Tax on Excess Designation

ITA
195(7.1)

Clause 73

New subsection 195(7.1) is added to the Act consequential to the introduction of new subsection 127.3(9). Subsection 127.3(9) allows a corporation that has made a public distribution of shares or debt obligations that carry a scientific research tax credit to elect to have the credit apply to the first purchaser as opposed to the first registered holder (other than brokers or dealers in securities). As a consequence of this election, various persons involved in the distribution to the public of the shares or debt obligations will be required to file information returns to substantiate the credit claimed by the first purchasers. New subsection 195(7.1) provides for an amount of Part VIII tax to be paid by such a person as a penalty where the total credits on information returns issued by him exceed the total credits available for distribution by him. The tax will be equal to the excess credits.

This amendment is applicable after September, 1983.

Excess RRSP Contributions

ITA
204.2(1)

Clause 74

Subsection 204.2(1) of the Act defines the amount of over- contributions to a registered retirement savings plan subject to the special tax payable under Part X.1 of the Act. The amendment to this section is strictly consequential on the introduction of new subsection 146(5.3) to the Act, which allows the deduction of a special contribution to a registered retirement savings plan in respect of taxable capital gains from qualified farm property. Paragraph 204.2(1)(e) is added for the 1984 and subsequent taxation years to ensure that this special contribution is not subject to the Part X.1 tax on over-contributions.

Property of Deferred Income Plans

ITA
206(2)(e.1)

Clause 75

Subsection 206(2) of the Act defines the term "foreign property" for the purposes of the special Part XI tax on the foreign property in excess of the allowed limits for registered pensions and certain other deferred income plans. Paragraph 206(2)(e.1) treats as foreign property any property (other than a share of a public corporation issued before 1984) that is convertible into or exchangeable for foreign property. The amendment to this paragraph excludes from foreign property any shares of a Canadian corporation listed on a prescribed stock exchange in Canada that are convertible into or exchangeable for foreign property where those shares have been acquired after 1983 upon the conversion or exchange of such publicly-traded shares pursuant to their terms and conditions on December 31, 1983.

Cross-Reference

ITA 208

An amendment is being made to the coming-into-force provision governing the special tax imposed on registered pension plans and other exempt persons in respect of certain Crown royalties. This amendment is made in clause 84 (see commentary thereunder).

Non-Arm's Length Sales of Shares by Non-Residents
ITA
212.1(1)

Clause 76

Section 212.1 of the Act ensures that non-residents cannot use non-arm's length reorganizations of their Canadian corporations to convert dividend distributions that would be subject to non-resident withholding tax under Part XIII of the Act into tax-free capital gains.

In corporate takeovers the acquiring corporation will usually have a right to purchase the shares of a target corporation before the actual acquisition occurs. Under paragraph 251(5)(b) of the Act, a person who holds a right to acquire, or to control the voting rights of, shares of a corporation is treated as owning the shares. This may result in the acquiring corporation being treated as controlling the target corporation and therefore as not dealing at arm's length with those persons from whom it is purchasing the shares. It is inappropriate for section 212.1 to be applied to the sale of shares of a Canadian corporation by a non-resident to a purchaser with whom he is deemed not to be dealing at arm's length simply because of the existence of such a right. The amendment to subsection 212.1(1) of the Act, applicable to dispositions of shares after April 10, 1978, corrects this problem.

Security for Taxes Payable

ITA
220(4), (4.1)
and (4.2)

Clause 77

Section 158 of the Act provides that where a taxpayer has received a notice of assessment from Revenue Canada, Taxation he must remit the assessed tax, interest and penalties then remaining unpaid within 30 days of the date of mailing of the assessment, whether or not he has objected to or appealed from the assessment. The Minister of National Revenue may, however, accept security for payment of the assessed tax under subsection 220(4) of the Act. This discretion would typically be exercised in circumstances of hardship. Subsection 220(4) is amended to permit the Minister to accept security for the payment of interest and penalties owing. As well, new subsection 220(4.1) will require the Minister to accept security for unpaid taxes, interest, and penalties in respect of which an objection or appeal is outstanding, provided that the security furnished is acceptable to the Minister. New subsection 220(4.2) ensures that the Minister must return security to the extent that the secured taxes, interest and penalties are no longer payable as a result of a successful appeal by the taxpayer to the courts. This new subsection provides a parallel to new subsection 164(4.1) which requires the refund of a tax paid in similar circumstances. Amended subsection 220(4) and new subsection 220(4.2) apply after February 15, 1984 and new subsection 220(4.1) applies to assessments objected to or appealed from after that date.

Clause 78

ITA
227(8)

Subsection 227(8) of the Act provides that any person who fails to deduct or withhold tax under the provisions of the Act or regulations is subject to a penalty in addition to interest on such unpaid taxes. The penalty is 10% of the amount that should have been deducted or withheld in the case of the withholding requirement under subsection 153(1) in respect of salary, wages and similar payment or under section 215 in respect of non-resident withholding tax. In any other case the penalty is equal to the entire amount that should have been withheld.

Subsection 227(8) is amended to clarify the date of application of the interest in respect of the unpaid tax. If the taxes withheld or deducted are not remitted to the Receiver General by the 15th day of the month immediately following the month in which the taxes should have been withheld or deducted, interest at the prescribed rate will start accruing from that date. Interest under this amendment will commence to be computed on February 16, 1984.

ITA
227(8.1)

New paragraph 227(8.1) is being added to the Act to provide that where a taxpayer fails to deduct or withhold tax on any amount paid to a non-resident person as required by section 215, the non-resident person will be jointly and severally liable with the taxpayer to pay any interest payable by the taxpayer pursuant to subsection 227(8). This amendment is applicable after February 15, 1984.

ITA
227(9)

Subsection 227(9) of the Act provides that a person who has deducted or withheld tax as required under the provisions of the Act or regulations but who fails to remit the tax withheld or deducted to the Receiver General will be subject to a penalty equal to 10% of the amount deducted or withheld plus interest on the amount so deducted or withheld.

This subsection is amended to clarify the date of application of the interest on the unremitted tax. If the taxes withheld or deducted are not remitted to the Receiver General by the 15th day of the month immediately following the month in which the taxes should have been withheld or deducted, interest at the prescribed rate will start accruing from the date.

The amendment to subsection 227(9) is effective after February 15, 1984.

Mailing Date

ITA
244(14)

Clause 79

Subsection 244(14) of the Act provides that the day of mailing of a notice of assessment or other notification shall, in the absence of any evidence to the contrary, be the date appearing thereon. For taxation years commencing after 1983, this subsection is amended to add a reference to new subsections 110(8.1) and (8.2) which provide that the Minister of National Revenue may, by notice sent by registered mail, designate a registered charity to be a charitable organization, private foundation or public foundation.

Tax Avoidance

Clause 80

ITA
246

Section 246 of the Act authorizes the Treasury Board to give such directions as it considers appropriate to counteract the improper avoidance or reduction of taxes under the Act. The authority so provided to the Treasury Board conflicts with the underlying purpose of the Canadian Charter of Rights and Freedoms and the section is accordingly being repealed effective February 16, 1984.

Definitions

Clause 81

ITA
248(1)

Subsection 248(1) of the Act defines many of the terms used in the Act.

"Active-Business" and "Canadian-controlled Private Corporation"

Subclauses 81(1) and (2)

The amendments to the definitions of "active business" and "Canadian-controlled private corporation", applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation, simply change the references to the provisions in section 125. These changes are strictly consequential on the amendments to section 125 relating to the small business deduction.

"Specified shareholder"

Subclause 81(3)

The addition of the definition "specified shareholder" to section 248 simply picks up a definition that was previously reflected in paragraph 125(9)(c) of the Act and makes the definition generally applicable for all purposes of the Act.

Subclause 81(4)

This sets out the effective date for the amendments to subsection 248(1) of the Act.

Taxation Years and Fiscal Period
ITA
249(2)

Clause 82

Subsection 249(2) of the Act provides that a reference in the Act to a taxation year ending in another year includes a reference to a taxation year ending co-incidentally with that other year. The amendment to the subsection provides that a reference to a fiscal period of a partnership ending in a taxation year includes a reference to a fiscal period of a partnership ending co-incidentally with that year. The amendment is applicable to taxation years ending in calendar years commencing after Royal Assent to the implementing legislation and is strictly consequential on the amendments to section 125 relating to the small business deduction.

Control of a Corporation

ITA
251(5)

Clause 83

Subsection 251(5) of the Act provides special rules for the purpose of determining whether or not persons and corporations are related or associated. Subsection 251(5) has been amended for taxation years ending in calendar years commencing after Royal Assent to the implementing legislation. The changes extend these special rules for the purpose of determining whether a corporation qualifies as "Canadian-controlled private corporation" and, as a consequence, whether it is eligible to claim the small business deduction provided in section 125 of the Act.

Part XII

ITA
208(1)

Clause 84

The tax imposed under Part XII of the Act applies to registered pension plans and other exempt persons that derive income from the operation of mines or from oil and gas production on which they are required to pay a royalty to taxable persons. This tax is designed to prevent the use of tax-exempt intermediaries to circumvent the provisions of the Act that operate to disallow or include in income various Crown royalties. The tax at a rate of 33 1/3% is based on the Crown royalties paid by the tax exempt person in such cases. Under the existing provision the tax is applicable only after December 31, 1983 with respect to income from properties acquired before December 12, 1979, the date on which the new tax was introduced. The amendment improves the grandfathering provision by extending this application date to January 1, 1990.

Petroleum and Gas Revenue Tax Act

PGRT
82(2)(f)

Clause 85

This amendment adds new paragraph 82(2)(f) to the Petroleum and Gas Revenue Tax (PGRT) Act to require a deduction of the cost of substances injected into a natural reservoir to assist in the recovery of petroleum or gas. Such costs are deductible for income tax purposes for the 1984 and subsequent taxation years by virtue of new paragraph 20(1)(mm) of the *Income Tax Act*.

For the 1984 taxation year, the deduction for PGRT purposes is the cost of substances injected after 1980 and before the end of the year that was deductible in 1984 under paragraph 20(1)(mm) of the *Income Tax Act*. For taxation years ending after 1984, the deduction is the costs of such substances that were injected during the year.

This provision is effective for the 1984 and subsequent taxation years.

Trust Income

ITA
104(6)(b)

Clause 86

Paragraph 104(6)(b) of the Income Tax Act was amended by subclause 60(2) of Bill C-139 to limit the deduction of certain income paid to the beneficiaries of a spousal trust. The effective date of the amendment to this paragraph is changed to remove the limitation where the income is paid by a trust created before November 13, 1981 to a person referred to in any of subparagraphs 110(1)(a)(i) to (vii) of the Income Tax Act.

Winding-up of a Corporation

ITA
88(1.1)

Clause 87

Clause 39(4) of Bill C-2 contained an amendment to subsection 88(1.1) of the Act concerning the flow-through of losses on the winding-up of a subsidiary corporation into its parent. The amendment was applicable to windings-up commencing in the 1983 and subsequent taxation years and inadvertently withdrew a special "grandfathering" transitional rule that was previously available for a winding-up in those circumstances in which control of the parent or subsidiary was last acquired before November 13, 1981. The transitional rule was provided in Bill C-139. This amendment to the coming-into-force provision in Bill C-2 restores the grandfathering protection.

Overseas Employment Tax Credit

ITA
122.3

Clause 88

The overseas employment tax credit, introduced in Bill C-2 is not available in respect of an individual's income from employment on a CIDA project. However, a special transitional rule provides that an employee working on a CIDA project who commences employment overseas before 1984 will be eligible for the credit on the same basis as other Canadians working abroad. The amendment to this transitional rule extends this ''grandfathering'' to those employees on projects who begin employment before 1987 in connection with a CIDA contract entered into on or before August 15, 1983, the date on which the rules relating to the overseas employment tax credit were made public.